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Accounts

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Revised as of January 1, 1986

CONTAINING
A CODIFICATION OF DOCUMENTS
OF GENERAL APPLICABILITY
AND FUTURE EFFECT

AS OF JANUARY 1, 1986

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Cite this Code **CFR**

thus: **4 CFR 2.1**

Explanation

The Code of Federal Regulations is a codification of the general and permanent rules published in the Federal Register by the Executive departments and agencies of the Federal Government. The Code is divided into 50 titles which represent broad areas subject to Federal regulation. Each title is divided into chapters which usually bear the name of the issuing agency. Each chapter is further subdivided into parts covering specific regulatory areas.

ISSUE DATES

Each volume of the Code is revised at least once each calendar year and issued on a quarterly basis approximately as follows:

Title 1 through Title 16	as of January 1
Title 17 through Title 27	as of April 1
Title 28 through Title 41	as of July 1
Title 42 through Title 50	as of October 1

The appropriate revision date is printed on the cover of each volume.

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The contents of the Federal Register are required to be judicially noticed (44 U.S.C. 1507). The Code of Federal Regulations is prima facie evidence of the text of the original documents (44 U.S.C. 1510).

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The Paperwork Reduction Act of 1980 (Pub. L. 96-511) requires Federal agencies to display an OMB control number with their information collection request. Many agencies have begun publishing numerous OMB control numbers as amendments to existing regulations in the CFR. These OMB numbers are placed as close as possible to the applicable recordkeeping or reporting requirements.

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An index to the text of "Title 3—The President" is carried within that volume.

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For a summary, legal interpretation, or other explanation of any regulation in this volume, contact the issuing agency. Inquiries concerning editing procedures and reference assistance with respect to the Code of Federal Regulations may be addressed to the Director, Office of the Federal Register, National Archives and Records Administration, Washington, D.C. 20408 (telephone 202-523-3517). Sales are handled exclusively by the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402 (telephone 202-783-3238).

John E. Byrne,
Director,
Office of the Federal Register.

January 2, 1986.

THIS TITLE

Title 4—Accounts is composed of one volume. All current regulations issued as of January 1, 1986, by the General Accounting Office (GAO) appear in Chapters I and II of this volume. The GAO regulations appearing in Chapter II are issued jointly with the Department of Justice. All current regulations issued by the General Accounting Office (CASB) appear in Chapter III.

In Chapter III, as a special feature for the benefit of the CFR users, the preambles in documents amending Parts 331, 332, 351, and 400-420 are included as supplements to their respective parts.

For this volume, Mildred L. Isler was Chief Editor. The Code of Federal Regulations publication program is under the direction of Martha B. Girard, assisted by Robert E. Jordan.

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SUBCHAPTER A—PERSONNEL SYSTEM

PART 2—PURPOSE AND GENERAL PROVISION

Sec.

2.1 Purpose, scope, and applicability.
2.2 References.
2.3 GAO Personnel Appeals Board.
2.4 Merit system principles.
2.5 Prohibited personnel practices.
2.6 Veterans' preference.

AUTHORITY: 31 U.S.C. 732.

SOURCE: 45 FR 68375, Oct. 15, 1980, unless otherwise noted.

§ 2.1 Purpose, scope, and applicability.

(a) This regulation establishes and sets forth the basic policy for the General Accounting Office (GAO) personnel system. Personnel management is a primary responsibility of all who plan, direct, or supervise the work of employees. The objective of personnel management is to contribute to the effective accomplishment of GAO's mission through proper acquisition, development, fair treatment, motivation, compensation and productive utilization of employees.

(b) Nothing in this regulation prohibits or restricts any lawful effort to achieve equal employment opportunity through affirmative action.

§ 2.2 References.

(a) Subchapters III and IV of Chapter 7 of Title 31 U.S.C.

(b) Title 5, United States Code.

[45 FR 68375, Oct. 15, 1980, as amended at 47 FR 56979, Dec. 22, 1982]

§ 2.3 GAO Personnel Appeals Board.

The General Accounting Office Personnel Appeals Board is established by 31 U.S.C. 751. This board will promulgate regulations providing for employee appeals and establishing its operating procedures.

[47 FR 56979, Dec. 22, 1982]

§ 2.4 Merit system principles.

(a) Merit personnel systems are based on the principle that an organization is best served by motivated, competent, honest and productive workers. In a merit system, employees are hired, promoted, rewarded, and retained on the basis of individual ability and fitness for employment without regard to race, color, sex, religion, age, or national origin. Central to this principle is the protection of employees from discrimination, improper political influence and personal favoritism.

(b) Equal employment opportunity is an integral part of every merit system. Affirmative action plans, designed to provide a work force reflective of the Nation's diversity, must assure that both in operation and results the merit system reflects equal opportunity at every step of the personnel process.

(c) GAO personnel systems shall embody the following merit system principles:

(1) Recruitment should be from qualified individuals from appropriate sources in an endeavor to achieve a work force from all segments of society, and selection and advancement should be determined solely on the basis of relative ability, knowledge, and skills, after fair and open competition which assures that all receive equal opportunity.

(2) All employees and applicants for employment should receive fair and equitable treatment in all aspects of personnel management without regard to political affiliation, race, color, religion, national origin, sex, marital status, age, or handicapping condition, and with proper regard for their privacy and constitutional rights.

(3) Equal pay should be provided for work of substantially equal value, with appropriate consideration of both national and local rates paid by employers in the private sector, and appropriate incentives and recognition should be provided for excellence in performance.

(4) All employees should maintain high standards of integrity, conduct, and concern for the public interest.

(5) The work force should be used efficiently and effectively.

(6) Employees should be retained on the basis of the adequacy of their performance, inadequate performance should be corrected, and employes

should be separated who cannot or will not improve their performance to meet required standards.

(7) Employees should be provided effective education and training in cases in which such education and training would result in better organizational and individual performance.

(8) Employees should be protected against arbitrary action, personal favoritism, or coercion from partisan political purposes and prohibited from using their official authority or influence for the purpose of interfering with or affecting the results of an election or a nomination for election.

(9) Employees should be protected against reprisal for the lawful disclosure of information which the employee reasonably believes evidences: a violation of any law, rule or regulation; or mismanagement, a gross waste of funds, an abuse of authority, or a substantial and specific danger to public health or safety.

§ 2.5 Prohibited personnel practices.

Any GAO employee who has authority to take, direct others to take, recommend, or approve any personnel action, shall not, with respect to such authority engage in the following prohibited personnel practices.

(a) *Discrimination.* GAO employees shall not discriminate for or against any employee or applicant for employment—

(1) On the basis of race, color, religion, sex, or national origin, as prohibited under section 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000 e-16);

(2) On the basis of age, as prohibited under section 12 and 15 of the Age Discrimination in Employment Act of 1967 (29 U.S.C. 631, 633a);

(3) On the basis of sex, as prohibited under section 6(d) of the Fair Labor Standards Act of 1938 (29 U.S.C. 206(d));

(4) On the basis of handicapping condition, as prohibited under section 501 of the Rehabilitation Act of 1973 (29 U.S.C. 791); or

(5) On the basis of marital status or political affiliation, as prohibited under any law, rule, or regulation.

(b) *Recommendations or statements.* GAO employees shall not solicit or consider any recommendation or statement, oral or written, with respect to any individual who requests or is under consideration for any personnel action unless such recommendation or statement is based on the personal knowledge or records of the person furnishing it and consists of—

(1) An evaluation of the work performance, ability, aptitude, or general qualifications of such individual, or

(2) An evaluation of the character, loyalty, or suitability of such individual.

(c) *Political activity.* GAO employees shall not coerce the political activity of any person (including the providing of any political contribution or service), or take any action against any employee or applicant for employment as a reprisal for the refusal of any person to engage in such political activity.

(d) *Compete for employment.* GAO employees shall not deceive or willfully obstruct any person with respect to such person's right to compete for employment.

(e) *Influencing competition.* GAO employees shall not influence any person to withdraw from competition for any position for the purpose of improving or injuring the prospects of any other person for employment.

(f) *Preference or advantage.* GAO employees shall not grant any preference or advantage not authorized by law, rule, or regulation to any employee or applicant for employment (including defining the scope or manner of competition or the requirements for any position) for the purpose of improving or injuring the prospects of any particular person for employment.

(g) *Relatives.* GAO employees who are serving as public officials (as defined in section 3110(a)(2) of title 5, United States Code) shall not appoint, employ, promote, advance, or advocate for appointment, employment, promotion, or advancement, in or to a GAO position any individual who is a relative (as defined in section 3110(a)(3) of title 5, United States Code) of such employee.

(h) *Reprisals.* GAO employees shall not take or fail to take a personnel action with respect to any employee or applicant for employment as a reprisal for—

(1) A disclosure of information by an employee or applicant which the employee or applicant reasonably believes evidences—

(i) A violation of any law, rule, or regulation, or

(ii) Mismanagement, a gross waste of funds, an abuse of authority, or a substantial and specific danger to public health or safety, if such disclosure is not specifically prohibited by law and if such information is not specifically required by Executive order to be kept secret in the interest of national defense or the conduct of foreign affairs; or

(2) A disclosure to the General Counsel of the GAO Personnel Appeals Board of information which the employee or applicant reasonably believes evidences—

(i) A violation of any law, rule, or regulation, or

(ii) Mismanagement, a gross waste of funds, an abuse of authority, or a substantial and specific danger to public health or safety.

(i) *Reprisals for appeals.* GAO employees shall not take or fail to take any personnel action against any employee or applicant for employment as a reprisal for the exercise of any appeal right granted by any law, rule, or regulation.

(j) *Discrimination for conduct.* GAO employees shall not discriminate for or against any employee or applicant for employment on the basis of conduct which does not adversely affect the performance of the employee or applicant or the performance of others; except that nothing in this paragraph shall prohibit an agency from taking into account in determining suitability or fitness any conviction of the employee or applicant for any crime under the laws of any State, or the District of Columbia, or of the United States.

(k) *Other personnel actions.* GAO employees shall not take or fail to take any other personnel action if the taking of or failure to take such action violates any law, rule or regulation implementing, or directly concerning, the merit system principles described in § 2.4.

(l) *Information to the Congress.* Nothing in this section shall be construed to authorize the withholding of information from the Congress or the taking of any personnel action against an employee who discloses information to the Congress.

§ 2.6 Veterans' preference.

(a) GAO will provide preference, for any individual who would be a preference eligible in the executive branch, in a manner and to an extent consistent with preference eligibles in the executive branch.

(b) Appeals from preference decisions will be heard by the GAO Personnel Appeals Board.

PART 3—EMPLOYMENT

Sec.
3.1 Appointment, promotion, and assignment.
3.2 Oath of office.
3.3 Assignments to and from States

AUTHORITY: 31 U.S.C. 732.

SOURCE: 45 FR 68376, Oct. 15, 1980, unless otherwise noted.

§ 3.1 Appointment, promotion, and assignment.

Employees of GAO shall be appointed, promoted and assigned solely on the basis of merit and fitness, but without regard to the provisions of Title 5, United States Code, governing appointments and other personnel actions in the competitive service.

§ 3.2 Oath of office.

The provisions of Subchapter II of Chapter 33 of Title 5, United States Code, and Office of Personnel Management implementing regulations apply to General Accounting Office employees.

§ 3.3 Assignments to and from States.

The provisions of Subchapter VI of Chapter 33 of Title 5, United States Code, and Office of Personnel Management implementing regulations apply to General Accounting Office employees.

PART 4—EMPLOYEE PERFORMANCE AND UTILIZATION

Sec.
4.1 Training.
4.2 Performance appraisal.
4.3 Removal for unacceptable performance.
4.4 Incentive awards.

AUTHORITY: 31 U.S.C. 732.

SOURCE: 45 FR 68376, Oct. 15, 1980, unless otherwise noted.

§ 4.1 Training.

The provisions of Chapter 41, of Title 5, United States Code, and Office of Personnel Management implementing regulations apply to General Accounting Office employees.

§ 4.2 Performance appraisal.

(a) The GAO shall develop one or more performance appraisal systems which provide for periodic appraisals of job performance of employees; encourages employee participation in establishing performance standards; and uses the results of performance appraisal as a basis for training, rewarding, reassigning, promoting, reducing in grade, retaining, and removing employees.

(b) Each performance appraisal system shall provide for—

(1) Establishing performance standards which will, to the maximum extent feasible, permit the accurate evaluation of job performance on the basis of job-related criteria (which may include the extent of courtesy demonstrated to the public) for each GAO employee.

(2) As soon as practicable, but not later than October 1, 1981, with respect to initial appraisal periods, and thereafter at the beginning of each following appraisal period, communicating to reach GAO employee the performance standards and the critical elements of the employee's position.

(3) Annually evaluating each employee during the appraisal period on such standards.

(4) Recognizing and rewarding employees whose performance so warrants.

(5) Assisting employees in improving unacceptable performance.

(6) Reassigning, reducing in grade, or removing employees who continue to have unacceptable performance but only after an opportunity to demonstrate acceptable performance.

§ 4.3 Removal for unacceptable performance.

GAO may reduce in grade/pay level or remove an employee for unacceptable performance in accordance with the provisions of this section.

(a) *Employee entitlement.* A GAO employee whose reduction in grade/pay level or removal is proposed under this section is entitled to—

(1) An advance written notice of the proposed action which identifies—

(i) Specifies instances of unacceptable performance by the employee on which the proposed action is based; and

(ii) The critical elements of the employee's position involved in each instance of unacceptable performance.

(2) Be represented by an attorney or other representative.

(3) A reasonable time to answer orally and in writing.

(4) A written decision which—

(i) Specific the instances of unacceptable performance by the employee on which the reduction in grade/pay level or removal is based.

(ii) Unless proposed by the Comptroller General or by a senior manager (e.g., the Deputy Comptroller General, an Assistant Comptroller General, or a Division or Office Director) has been concurred in by an employee who is in a higher position than the employee who proposed the action.

(b) *Decisions to retain, reduce in grade/pay level or remove.* The decision to retain, reduce in grade or remove a GAO employee—

(1) Shall be made within 30 days after the date of expiration of the notice period, and

(2) In the case of reduction in grade/pay level or removal, may be based only on those instances of unacceptable performance by the employee—

(i) Which occurred during the 1-year period ending on the date of the notice of the proposed action.

(ii) For which the notice and other requirements of this section are complied with.

(c) *Performance improvement.* If because of performance improvement by the employee during the notice period, the employee is not reduced in grade/pay level or removed, and the employee's performance continues to be acceptable for 1 year from the date of advance written notice, any records shall be retained only as prescribed by other recordkeeping requirements, such as grievances, adverse action appeals, or discrimination complaints. In these circumstances any entry or notation of unacceptable performance shall be removed from the employee's official personnel folder and maintained in separate files to be used only in connection with an employee initiated complaint.

(d) *Appeals.* A GAO employee who has been reduced in grade/pay level or removed under this section is entitled to appeal the action to the GAO Personnel Appeals Board.

(e) *Nonapplicability.* This section does not apply to—

(1) The reduction to the grade/pay level previously held of a supervisor or manager who has not completed the trail period

(2) The reduction in grade/pay level or removal of a GAO employee who is serving a trial period under an initial appointment or who has not completed 1 year of current continuous employment under other than a temporary appointment limited to 1 year or less

(3) Employees in the GAO Senior Executive Service.

§ 4.4 Incentive awards.

The provisions of Chapter 45 of Title 5, United States Code and Office of Personnel Management implementing regulations apply to General Accounting Office employees.

PART 5—COMPENSATION

Sec.

5.1 Pay.
5.2 Grade and pay retention.
5.3 Merit pay.
5.4 Pay administration.
5.5 Travel, transportation, and subsistence.
5.6 Allowances.

AUTHORITY: 31 U.S.C. 732.

SOURCE: 45 FR 68377, Oct. 15, 1980, unless otherwise noted.

§ 5.1 Pay.

(a) *Pay principles.* Pay of the employees of GAO shall be fixed by the Comptroller General consistent with the principles that—

(1) There be equal pay for work of substantially equal value.

(2) Pay distinctions be maintained in keeping with work and performance distinctions.

(3) Pay rates be comparable with private enterprise pay rates for the same levels of work.

(4) Pay levels be interrelated to the General Schedule.

(b) *Pay rates.* (1) The Comptroller General shall publish a schedule of pay rates which shall apply to GAO employees. Except as provided in paragraph (b)(2) of this section, and regulations for the GAO Senior Executive Service, the highest rate under such schedule shall not exceed the highest rate of basic pay payable for grade GS-15 under the General Schedule.

(2) Such schedule may provide for rates which do not exceed the maximum rate payable for grade GS-18 of the General Schedule for up to one hundred employees, reduced by the number of employees who are in the GAO Senior Executive Service, other than those in such service pursuant to 31 U.S.C. 733(c).

(c) Pay adjustments. Except as provided in regulations for the GAO Senior Executive Service and the Merit Pay System, the pay of GAO employees shall be adjusted at the same time and to the same extent as rates of basic pay are adjusted for the General Schedule.

[45 FR 68377, Oct. 15, 1980, as amended at 47 FR 56979, Dec. 22, 1982]

§ 5.2 Grade and pay retention.

(a) *Change of positions.* Any GAO employee who is placed in a lower grade position as a result of a reduction-in-force may be entitled to the retained grade of the higher position he or she previously held. The employee receives this entitlement (which is for a period of 2 years) if he or she has served for at least 52 consecutive weeks in one or more positions at a grade or grades higher than the new position. The 2-year period begins on the date of placement to the lower grade position.

(b) *Reclassification.* Any GAO employee who is in a position which is reduced in grade is entitled to have the grade of such position before reduction be treated as the retained grade of such employee for the 2-year period beginning on the date of reduction in grade. However, this section shall not apply to any reduction in the grade of a position which had not been classified at the higher grade for a continuous period of at least 1 year immediately before such reduction.

(c) *Retained grade.* For the 2-year period referred to in paragraphs (a) and (b) of this section, the retained grade of GAO employees shall be treated as the grade of the employee's position for all purposes (including pay and pay administration, retirement, life insurance and eligibility for training and promotion) except—

(1) For purposes of § 5.2(a).

(2) For purposes of applying any reduction-in-force procedures.

(3) For purposes of determining whether the employee is covered by a merit pay system.

(4) For such other purposes as the Comptroller General may provide by regulation.

(d) *Termination of retained grade.* The foregoing provisions of this section shall cease to apply to any GAO employee who—

(1) Has a break in service of 1 workday or more;

(2) Is demoted for personal cause or at the employee's request;

(3) Is placed in, or declines, a reasonable offer of, a position the grade of which is equal or higher than the retained grade; or

(4) Elects in writing to have the benefits of this chapter terminate.

(e) *Pay retention.* (1) Any GAO employee: who ceases to be entitled to a retained grade by reason of the expiration of the 2-year period; or who (but for this paragraph) would be subject to a reduction in pay under circumstances prescribed by the Comptroller General by regulation to warrant the application of this paragraph is entitled to—

(2) Basic pay at a rate equal to the employee's allowable former rate of basic pay, plus 50 percent of the amount of each increase in the maximum rate of basic pay payable for the employee's position immediately after such reduction in pay if such allowable former rate exceeds such maximum rate for such grade.

(f) *"Allowable former rate of basic pay."* This means the lower of—

(1) The rate of basic pay payable to the employee immediately before the reduction in pay; or

(2) 150 percent of the maximum rate of basic pay payable for the grade of the employee's position immediately after such reduction in pay.

(g) *Termination of retained pay.* The pay retention provisions in § 5.2(e) shall cease to apply to a GAO employee who—

(1) Has a break in service of 1 workday or more.

(2) Is entitled by operation of §§ 5.1, 5.2, and 5.3 to a rate of basic pay which is equal to or higher than, or declines a reasonable offer of a position the rate of basic pay for which is equal to or higher than, the rate to which the employee is entitled under § 5.2(e); or

(3) Is demoted for personal cause or at the employee's request.

(h) *Remedial actions.* Under regulations prescribed by the Comptroller General, Personnel shall—

(1) Obtain and make available to employees receiving benefits under this section, information on vacancies in other Federal agencies.

(2) Take such steps as may be appropriate to assure employees receiving benefits under this section have the opportunity to obtain necessary qualifications for the selection to positions which would minimize the need for the application of this section; and

(3) Establish a program under which employees receiving benefits under this section are given priority in the consideration for or placement in positions which are equal to their retained grade or pay.

(i) *Appeals.* In the case of the termination of any benefits to a GAO employee under this section on the grounds that such employee declined a reasonable offer of a position the grade or pay of which was equal to or greater than their retained grade or pay, after administrative remedies have been exhausted, such termination may be appealed to the GAO Personnel Appeals Board under procedures prescribed by the Board.

§ 5.3 Merit pay.

The Comptroller General may promulgate regulations establishing a merit pay system for such employees of the General Accounting Office as the Comptroller General considers appropriate. The merit pay system shall be designed to carry out purposes consistent with those set forth in section 5401(a) of Title 5, United States Code, which provides—

> *§ 5401. Purpose*
>
> (a) It is the purpose of this chapter to provide for—
>
> (1) A merit pay system which shall—
>
> (A) Within available funds, recognize and reward quality performance by varying merit pay adjustments;
>
> (B) Use performance appraisals as the basis for determining merit pay adjustments;
>
> (C) Within available funds, provide for training to improve objectivity and fairness in the evaluation of performance; and
>
> (D) Regulate the costs of merit pay by establishing appropriate control techniques; and
>
> (2) A cash award program which shall provide cash awards for superior accomplishment and special service.

§ 5.4 Pay administration.

The provisions of Chapter 55 of Title 5, United States Code and the Office of Personnel Management implementing regulations apply to General Accounting Office employees.

§ 5.5 Travel, transportation, and subsistence.

The provisions of Chapter 57 of Title 5, United States Code and the implementing regulations for the Executive Branch apply to General Accounting Office employees.

§ 5.6 Allowances.

The provisions of Chapter 59 of Title 5, United States Code and the implementing regulations for the Executive Branch apply to General Accounting Office employees.

PART 6—ATTENDANCE AND LEAVE

AUTHORITY: 31 U.S.C. 732.

§ 6.1 Applicable law and regulations.

The provision of Subpart E, Title 5, United States Code and the Office of Personnel Management implementing regulations regarding "Attendance and Leave" apply to General Accounting Office employees. This includes hours of work, annual leave, sick leave, and other paid leave.

[45 FR 68378, Oct. 15, 1980, as amended at 47 FR 56979, Dec. 22, 1982]

PART 7—PERSONNEL RELATIONS AND SERVICES

Sec.
7.1 Labor management relations.
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7.7 Other appeals and grievances.
7.8 Services to employees.

AUTHORITY: 31 U.S.C. 732.

SOURCE: 45 FR 68378, Oct. 15, 1980, unless otherwise noted.

§ 7.1 Labor management relations.

(a) *Policy.* Each employee of GAO has the right, freely and without fear of penalty or reprisal, to form, join, or assist an employee organization, or to refrain from such activity.

(b) *Labor relations program.* A labor relations program consistent with Chapter 71 of Title 5, United States Code will be developed for the General Accounting Office.

§ 7.2 Equal employment opportunity.

(a) *Policy.* All personnel actions affecting employees or applicants for employment in GAO shall be taken without regard to race, color, religion, age, sex, national origin, political affiliation, marital status or handicapping condition.

(b) *Equal opportunity recruiting program.* GAO shall conduct continuing programs for the recruitment of members of minorities and women for positions in GAO in a manner designed to eliminate underrepresentation of minorities and women in the various categories of employment in GAO. Special efforts will be directed at recruiting in minority communities, in educational institutions, and from other sources from which minorities can be recruited. GAO will conduct a continuing program of evaluation and oversight of such recruiting programs to determine their effectiveness in eliminating minority and women underrepresentation.

(c) *Statutory rights and remedies.* Nothing in this order shall be construed to abolish or diminish any right or remedy granted to employees of or applicants for employment in GAO—

(1) By section 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000e-16);

(2) By sections 12 and 15 of the Age Discrimination in Employment Act of 1967 (29 U.S.C. 631, 633a);

(3) By section 6(d) of the Fair Labor Standards Act of 1938 (29 U.S.C. 206(d));

(4) By sections 501 and 505 of the Rehabilitation Act of 1973 (29 U.S.C. 791, 794a); or

(5) By any other law prohibiting discrimination in Federal employment on the basis of race, color, religion, age, sex, national origin, political affiliation, marital status or handicapping condition.

(d) *Authorities granted thereunder to the Equal Employment Opportunity Commission, Office of Personnel Management, the Merit Systems Protection Board, or any other agency in the executive branch concerning oversight and appeals shall be exercised by the GAO Personnel Appeals Board.* Other responsibilities shall be exercised by the Comptroller General.

§ 7.3 Political activities.

(a) *Political contributions and services.* GAO employees are not obliged, by reason of employment, to contribute to a political fund or to render political service, and they may not be removed or otherwise prejudiced for refusal to do so.

(b) *Use of authority or influence.* GAO employees may not use their official authority or influence to coerce the political action of a person or body.

(c) *Political contributions.* GAO employees may not request or receive from, or give to, an employee, a Member of Congress, or an officer of the uniformed service a thing of value for political purposes. An employee who violates this section shall be removed from employment. It should be noted, however, that this does not preclude GAO employees from making a financial contribution to a political party or organization.

(d) *Elections; political campaigns.* GAO employees may not use their official authority or influence for the purpose of interfering with or affecting the results of an election; or take part in political management or in political campaigns.

(1) Employees retain the right to vote as they choose and to express their opinions on political subjects and candidates.

(2) An employee who violates this section shall be removed from employment. However, if the GAO Personnel Appeals Board, finds by unanimous vote that the violation does not warrant removal, a penalty of not less than 30-days suspension without pay shall be imposed by direction of the GAO Personnel Appeals Board.

(e) *Nonpartisan political activity permitted.* Section 7.3(d) does not prohibit political activity in connection with (1) a nonpartisan campaign and election (where none of the candidates represent a political party which had candidates for presidential elector in the last presidential election), or (2) a question which is not specifically identified with a National or State political party or political party of a territory or possession of the United States. (This includes questions relating to constitutional amendments, referendums, approval of municipal ordinances and others of a similar nature.)

(f) *Political activity permitted in certain municipalities.* The Comptroller General may permit GAO employees to take an active part in political management and political campaigns involving the municipality or other political subdivision in which they reside, to the extent the Comptroller General considers it to be in their domestic interest, when—

(1) The municipality or political subdivision is in Maryland or Virginia and in the immediate vicinity of the District of Columbia, or is a municipality in which the majority of voters are employed by the United States Government; and

(2) The Comptroller General determines that because of special or unusual circumstances which exist in the municipality or political subdivision it is in the domestic interest of the employees to permit that political participation.

§ 7.4 Employment limitations, foreign gifts and decorations, and misconduct.

The provisions of Subchapters II, IV, and V of Chapter 73 of title 5, United States Code and implementing regulations thereunder continue to apply to this office.

§ 7.5 Adverse actions: Suspensions for 14 days or less.

(a) *Policy.* A GAO employee may be suspended for 14 days or less for such cause as will promote the efficiency of GAO (including discourteous conduct to the public confirmed by an immediate supervisor's report of four such instances within any 1-year period or any other pattern of discourteous conduct). Suspension means placing an employee, for disciplinary reasons, temporarily in a status without duties and pay.

(b) *Employee entitlement.* An employee against whom a suspension for 14 days or less is proposed is entitled to—

(1) An advance written notice stating the specific reasons for the proposed action;

(2) A reasonable time to answer orally and in writing and to furnish affidavits and other documentary evidence in support of the answer;

(3) Be represented by an attorney or other representative; and

(4) A written decision and the specific reasons therefore at the earliest practicable date.

(c) *Documentation.* Copies of the notice of proposed action, the answer of the employee if written, a summary thereof if made orally, the notice of decision and reasons therefor, and any order effecting the suspension, together with any supporting material, shall be maintained by Personnel and shall be furnished to the employee affected upon the employee's request.

(d) *Nonapplicability.* This section is not applicable to—(1) An employee who is serving a trial period under an initial appointment in GAO or who has not completed 1 year of current continuous employment in the same or similar positions in GAO under other than a temporary appointment limited to 1 year or less.

(2) A suspension in the interest of national security.

§ 7.6 Adverse actions: Removal, suspension for more than 14 days, reduced in grade, reduced in pay or furloughed for 30 days or less.

(a) *Policy.* A GAO employee may be removed, suspended for more than 14 days, reduction in grade or pay, or furlough for 30 days or less for such cause as will promote the efficiency of GAO. Furloughed means placing an employee in a temporary status without duties and pay because of lack of work or funds or other nondisciplinary reasons.

(b) *Employee entitlement.* An employee against whom an action is proposed under this section is entitled to—

(1) At least 30 days' advance written notice, unless there is reasonable cause to believe the employee has committed a crime for which a sentence of imprisonment may be imposed, stating the specific reasons for the proposed action.

(2) A reasonable time to answer orally and in writing and to furnish affidavits and other documents in support of the answer.

(3) Be represented by an attorney or other representative; and

(4) A written decision and the specific reasons therefor at the earliest practicable date.

(c) *Appeals.* After administrative remedies have been exhausted, an employee against whom an action is taken under this section is entitled to appeal to the GAO Personnel Appeals Board.

(d) *Documentation*. Copies of the notice of proposed action, the answer of the employee if written, a summary thereof when made orally, the notice of decision and reasons therefor, and any order affecting an action covered by this section, together with any supporting material, shall be maintained by Personnel and shall be furnished to the GAO Personnel Appeals Board upon its request and to the employee affected upon the employee's request.

(e) *Nonapplicability*. This section does not apply to—

(1) Employees who are serving a trial period under an initial appointment or who has not completed 1 year of current continuous employment under other than a temporary appointment limited to 1 year or less.

(2) A suspension or removal of an employee in the interests of national security.

(3) A reduction in force.

(4) The reduction in grade of a supervisor or manager who has not completed the probationary period.

(5) A reduction in grade or removal for unacceptable performance under Part 4.

(6) An action ordered by the GAO Personnel Appeals Board.

§ 7.7 Other appeals and grievances.

The personnel system shall provide procedures for the processing of complaints and grievances which are not otherwise provided for.

§ 7.8 Services to employees.

The provisions of Chapter 79 of Title 5, United States Code, and the Office of Personnel Management implementing regulations apply to General Accounting Office employees.

PART 8—INSURANCE AND ANNUITIES

AUTHORITY: 31 U.S.C. 732.

§ 8.1 Applicable law and regulations.

The provisions of Subpart G, Title 5, United States Code and implementing regulations for the Executive Branch covering compensation for work injuries, retirement, unemployment compensation, life insurance, and health insurance apply to General Accounting Office employees.

[45 FR 68380, Oct. 15, 1980, as amended at 47 FR 56979, Dec. 22, 1982]

PART 9—SENIOR EXECUTIVE SERVICE

AUTHORITY: 31 U.S.C. 733.

§ 9.1 GAO Senior Executive Service.

(a) The Comptroller General may promulgate regulations establishing a General Accounting Office Senior Executive Service which meets the requirements set forth in section 3131 of Title 5, United States Code, which provides—

> § 3131 The GAO Senior Executive Service
>
> The Senior Executive Service shall be administered so as to—
>
> (1) Provide for a compensation system, including salaries, benefits, and incentives, and for other conditions of employment, designed to attract and retain highly competent senior executives;
>
> (2) Ensure that compensation, retention, and tenure are contingent on executive success which is measured on the basis of individual and organizational performance (including such factors as improvements in efficiency, productivity, quality of work or service, cost efficiency, and timeliness of performance and success in meeting equal employment opportunity goals);
>
> (3) Assure that senior executives are accountable and responsible for the effectiveness and productivity of employees under them;
>
> (4) Recognize exceptional accomplishment;
>
> (5) Enable the head of an agency to reassign senior executives to best accomplish the agency's mission;
>
> (6) Provide for severance pay, early retirement, and placement assistance for senior executives who are removed from the Senior Executive Service for nondisciplinary reasons;
>
> (7) Protect senior executives from arbitrary or capricious actions;
>
> (8) Provide for program continuity in the management of GAO programs;
>
> (9) Maintain a merit personnel system free of prohibited personnel practices;
>
> (10) Ensure accountability for honest, economical, and efficient Government;
>
> (11) Ensure compliance with all applicable personnel laws, rules, and regulations, in-

cluding those related to equal employment opportunity, political activity, and conflicts of interest;

(12) Provide for the initial and continuing systematic development of highly competent senior executives;

(13) Provide for an executive system which is guided by the public interest and free from improper political interference; and

(14) Appoint career executives to fill Senior Executive Service positions to the extent practicable, consistent with the effective and efficient implementation of agency policies and responsibilities.

(b) Requirements for positions included in the GAO Senior Executive System. The GAO Senior Executive Service may include—

(1) The 100 positions authorized by 31 U.S.C. 732(c)(4);

(2) The position of the General Counsel authorized by 31 U.S.C. 731(c);

(3) The 5 positions authorized by 31 U.S.C. 731(d); and

(4) The 10 positions authorized by 31 U.S.C. 731(e)(2).

[45 FR 68380, Oct. 15, 1980, as amended at 47 FR 56979, Dec. 22, 1982]

PART 11—RECOGNITION OF ATTORNEYS AND OTHER REPRESENTATIVES

Sec.

11.1 Right to representation before the General Accounting Office.
11.2 Practice by attorneys.
11.3 Authority to represent in payment cases.
11.4 Authority to represent in other cases.
11.5 Revocation of authority to represent.

AUTHORITY: 31 U.S.C. 711.

SOURCE: 41 FR 35155, Aug. 20, 1976. Redesignated at 45 FR 68374, Oct. 15, 1980, unless otherwise noted.

§ 11.1 Right to representation before the General Accounting Office.

Each person having a claim or other rights assertable in the General Accounting Office may pursue such claim or right individually or through an attorney or other representative.

§ 11.2 Practice by attorneys.

Any person who is a member in good standing of the bar of the Supreme Court of the United States or of the highest court of any State, territory, or the District of Columbia, and is not under any order of any court suspending, enjoining, restraining, disbarring, or otherwise restricting him in the practice of law, may represent others before the General Accounting Office.

§ 11.3 Authority to represent in payment cases.

In the prosecution of claims involving payments to be made by the United States, a proper power of attorney is required before an attorney or other representative may be recognized. A power of attorney from the principal may also be requested in other cases.

§ 11.4 Authority to represent in other cases.

When an attorney acting in a representative capacity appears in person or signs a document submitted to the General Accounting Office in connection with a matter other than one involving a payment to be made by the United States, his personal appearance or signature shall constitute a representation that he is authorized and qualified to represent the particular party in whose behalf he acts. In the case of representatives other than attorneys, a simple written declaration from the principal will be accepted as evidence of the authority of the representative to act on behalf of the principal.

§ 11.5 Revocation of authority to represent.

Prior to the conclusion of action by the General Accounting Office on a matter in which a principal is represented by another person whose authority to act is established under either § 11.3 or § 11.4, the principal may revoke the authority of his representative. Such revocation is not effective unless it is in writing and signed by the principal and until the written revocation is received by the General Accounting Office. Upon notification of the death of the principal during the pendency of any matter involving representation of the principal by an attorney or other party, the General Accounting Office will consider the representative's authority to have been automatically revoked.

SUBCHAPTER B—GENERAL PROCEDURES

PART 21—BID PROTEST REGULATIONS

Sec.

21.0 Definitions.
21.1 Filing of protest.
21.2 Time for filing.
21.3 Notice of protest, submission of agency report and time for filing of comments on report.
21.4 Withholding of award and suspension of contract performance.
21.5 Conference.
21.6 Remedies.
21.7 Time for decision by the General Accounting Office.
21.8 Express Option.
21.9 Effect of judicial proceedings.
21.10 Signing and distribution of decisions.
21.11 Nonstatutory protests.
21.12 Request for reconsideration.

AUTHORITY: 31 U.S.C. 3551-3556.

SOURCE: 49 FR 49419, Dec. 20, 1984, unless otherwise noted.

§ 21.0 Definitions.

(a) "Interested party" means an actual or prospective bidder or offeror whose direct economic interest would be affected by the award of a contract or by the failure to award a contract.

(b) "Federal agency" means any executive department or independent establishment in the executive branch, including any wholly owned government corporation, and any establishment in the legislative or judicial branch, except the Senate, the House of Representatives and the Architect of the Capitol and any activities under his direction.

(c) "Contracting agency" means a federal agency which has awarded or proposes to award a contract under a protested procurement.

(d) All "days" referred to are deemed to be "working days" of the federal government except in § 21.4, where the statutory language is repeated. Except as otherwise provided, in computing a period of time prescribed by these regulations, the day from which the designated period of time begins to run shall not be counted, but the last day of the period shall be counted unless that day is not a working day of the federal government, in which event the period shall include the next working day. Time for filing any document or copy thereof with the General Accounting Office expires at 5:30 p.m. Eastern Standard Time or Eastern Daylight Savings Time as applicable on the last day on which such filing may be made.

(e) "Adverse agency action" is any action or inaction on the part of a contracting agency which is prejudicial to the position taken in a protest filed with the agency. It may include but is not limited to: a decision on the merits of a protest; a procurement action such as the opening of bids or receipt of proposals, the award of a contract, or the rejection of a bid despite the pendency of a protest; or contracting agency acquiescence in and active support of continued and substantial contract performance.

§ 21.1 Filing of protest.

(a) An interested party may protest to the General Accounting Office a solicitation issued by or for a federal agency for the procurement of property or services, or the proposed award or the award of such a contract. After an interested party protests a particular procurement or proposed procurement of automated data processing equipment and services to the General Services Administration Board of Contract Appeals under section III(h) of the Federal Property and Administrative Services Act of 1949 (40 U.S.C. 759(h)) and while that protest is pending before the Board that procurement or proposed procurement may not be the subject of a protest to the General Accounting Office. An interested party who has filed a protest with the Board may not protest the same matter to the General Accounting Office.

(b) Protests must be in writing and addressed as follows: General Counsel, General Accounting Office, Washington, D.C. 20548, Attention: Procurement Law Control Group.

(c) A protest filed with the General Accounting Office shall:

(1) Include the name, address and telephone number of the protester.

(2) Include an original signed by the protester or its representative, and at least one copy,

(3) Identify the issuing agency and the solicitation and/or contract number,

(4) Set forth a detailed statement of the legal and factual grounds of protest including copies of relevant documents,

(5) Specifically request a ruling by the Comptroller General of the United States (Comptroller General), and

(6) State the form of relief requested.

(d) The protester shall furnish a copy of the protest (including relevant documents not issued by the contracting agency) to the individual or location designated by the contracting agency in the solicitation for receipt of protests. If there is no designation in the solicitation, the protester shall furnish a copy of the protest to the contracting officer. The designated individual or location, or if applicable, the contracting officer must receive a copy of the protest no later than 1 day after the protest is filed with the General Accounting Office. The protest document must indicate that a copy has been furnished or will be furnished within 1 day to the appropriate individual or location.

(e) No formal briefs or other technical forms of pleading or motion are required. Protest submissions should be concise, logically arranged, and clearly state legally sufficient grounds of protest.

(f) A protest filed with the General Accounting Office may be dismissed for failure to comply with any of the requirements of this section.

§ 21.2 Time for filing.

(a)(1) Protests based upon alleged improprieties in a solicitation which are apparent prior to bid opening or the closing date for receipt of initial proposals shall be filed prior to bid opening or the closing date for receipt of initial proposals. In procurements where proposals are requested, alleged improprieties which do not exist in the initial solicitation but which are subsequently incorporated into the solicitation must be protested not later than the next closing date for receipt of proposals following the incorporation.

(2) In cases other than those covered in paragraph (a)(1) of this section, protests shall be filed not later than 10 days after the basis of protest is known or should have been known, whichever is earlier.

(3) If a protest has been filed initially with the contracting agency, any subsequent protest to the General Accounting Office filed within 10 days of formal notification of or actual or constructive knowledge of initial adverse agency action will be considered, provided the initial protest to the agency was filed in accordance with the time limits prescribed in paragraph (a)(1) and (a)(2) of this section, unless the contracting agency imposes a more stringent time for filing, in which case the agency's time for filing will control. In cases where an alleged impropriety in a solicitation is timely protested to a contracting agency, any subsequent protest to the General Accounting Office must be filed within the 10-day period provided by this paragraph.

(b) The term "filed" regarding protests to the General Accounting Office means receipt of the protest submission in the General Accounting Office.

(c) The General Accounting Office, for good cause shown, or where it determines that a protest raises issues significant to the procurement system, may consider any protest which is not filed timely.

§ 21.3 Notice of protest, submission of agency report and time for filing of comments on report.

(a) The General Accounting Office shall notify the contracting agency by telephone within 1 day of the filing of a protest, and shall promptly mail confirmation of that notification to the contracting agency. The contracting agency shall immediately give notice of the protest to the contractor if award has been made or, if no award has been made, to all bidders or offerors who appear to have a substantial and reasonable prospect of receiving an award if the protest is denied. The contracting agency shall furnish copies of the protest submissions to such parties with instructions to communicate further directly with the General Accounting Office. Copies of any such communications from any such parties shall be furnished to the contracting agency.

(b) Material submitted by a protester will not be withheld from any interested party outside the government or from any federal agency which may be involved in the protest except to the extent that the withholding of information is permitted or required by law or regulation. If the protester considers that the protest contains material which should be withheld, a statement advising of this fact must be affixed to the front page of the protest submission and the allegedly protected information must be so identified wherever it appears.

(c) The contracting agency shall file a complete report on the protest with the General Accounting Office within 25 days from the date of the telephone notice of the protest from the General Accounting Office. The report shall contain copies of relevant documents including, as appropriate: the protest, the bid or proposal submitted by the protester, the bid or proposal of the firm which is being considered for award, or whose bid or proposal is being protested, the solicitation, including the specifications or portions relevant to the protest, the abstract of bids or offers or relevant portions, any other documents that are relevant to the protest, and the contracting officer's statement setting forth findings, actions, recommendations and any additional evidence or information deemed necessary in determining the validity of the protest. The statement shall be fully responsive to all allegations of the protest which the agency contests. Pursuant to section 3553(f) of the Competition In Contracting Act of 1984, Pub. L. 98-369, the contracting agency shall simultaneously furnish a copy of the report to the protester and interested parties who have responded to the notice given under paragraph (a) of this section. Copies of reports furnished to such parties shall include relevant documents that would not give the party a competitive advantage and that the party is otherwise authorized by law or regulation to receive. If documents are withheld from any of the parties, the agency must include in the report filed with the General Accounting Office and in the copies of the report provided to the protester and interested parties a list of the withheld documents. The copy of the report filed with the General Accounting Office shall also identify the parties who have been furnished copies of the report.

(d) The contracting agency may request, in writing, an extension of the 25-day report submission time period. The request shall set forth the reasons for which the extension is needed. The General Accounting Office will determine, in writing, whether the specific circumstances of the protest require a period longer than 25 days for the submission of the report and, if so, will set a new date for the submission of the report. Extensions are to be considered exceptional and will be granted sparingly. The agency should make its request for an extension as promptly as possible to permit it to submit a timely report should the General Accounting Office deny the request.

(e) Comments on the agency report shall be filed with the General Accounting Office within 7 days after receipt of the report, with a copy furnished by the commenting party to the contracting agency and other participating interested parties. Failure of the protester to file comments, or to file a statement requesting that the case be decided on the existing record, or to request an extension under this section within the 7-day period will result in dismissal of the protest. The General Accounting Office upon a showing that the specific circumstances of the protest require a period longer than 7 days for the submission of comments on the agency report, may set a new date for the submission of such comments. Extensions are to be considered exceptional and will be granted sparingly.

(f) Notwithstanding any other provision of this section, when on its face a protest does not state a valid basis for protest or is untimely (unless the protest is to be considered pursuant to § 21.2(c)) or otherwise not for consideration by the General Accounting Office, it will summarily dismiss the protest without requiring the submission of an agency report. When the propriety of a dismissal becomes clear only after information is provided by the contracting agency or is otherwise obtained by the General Accounting Office, it will dismiss the protest at that time. If the General Accounting Office has dismissed the protest, it will notify the contracting agency that a report need not be submitted. Among the protests which may be dismissed without consideration of the merits are those concerning the following:

(1) Contract Administration. The administration of an existing contract is within the discretion of the contracting agency. Disputes between a contractor and the agency are resolved pursuant to the disputes clause of the contract and the Contract Disputes Act of 1978. 41 U.S.C. 601-13.

(2) Small Business Size Standards and Standard Industrial Classification. Challenges of established size standards or the size status of particular firms, and challenges of the selected standard industrial classification are for review solely by the Small Business Administration. 15 U.S.C. 637(b)(6); 13 CFR 121.3-6 (1984).

(3) Small Business Certificate of Competency Program. Any referral made to the Small Business Administration pursuant to section 8(b)(7) of the Small Business Act, or any issuance of a certificate of competency or refusal to issue a certificate under such section is not reviewed by the General Accounting Office absent a showing of possible fraud or bad faith on the part of government officials.

(4) Procurements under section 8(a) of the Small Business Act. Since contracts are let under section 8(a) of the Small Business Act to the Small Business Administration at the contracting officer's discretion and on such terms as agreed upon by the procuring agency and the Small Business Administration, the decision to place or not to place a procurement under the 8(a) program and the award of an 8(a) subcontract are not subject to review absent a showing of possible fraud or bad faith on the part of government officials or that regulations may have been violated. 15 U.S.C. 637(a).

(5) Affirmative Determination of Responsibility by the Contracting Officer. Because a determination that a bidder or offeror is capable of performing a contract is based in large measure or subjective judgments which generally are not readily susceptible of reasoned review, an affirmative determination of responsibility will not be reviewed, absent a showing that such determination was made fraudulently or in bad faith or that definitive responsibility criteria in the solicitation were not met.

(6) Procurement Protested to the General Services Administration Board of Contract Appeals. Interested parties may protest a procurement or proposed procurement of automated data processing equipment and services to the General Services Administration Board of Contract Appeals. After a particular procurement or proposed procurement is protested to the Board, the procurement may not, while the protest is before the Board, be the subject of a protest to the General Accounting Office. An interested party who has filed a protest with the Board may not protest the same matter to the General Accounting Office. 40 U.S.C. 759(h), as amended by section 2713 of the Competition In Contracting Act of 1984, Pub. L. 98-369.

(7) Protests not filed either in the General Accounting Office or the contracting agency within the time limits set forth in § 21.2.

(8) Procurements by Agencies Other Than Federal Agencies as Defined by Section 3 of the Federal Property and Administrative Services Act of 1949, 40 U.S.C. 472. Protests of procurements of proposed procurements by such agencies (e.g., U.S. Postal Service, Federal Deposit Insurance Corporation, nonappropriated fund activities) are beyond the General Accounting Office bid protest jurisdiction as established in section 2741 of the Competition In Contracting Act of 1984, Pub. L. 98-369.

(9) Walsh-Healey Public Contracts Act. Challenges of the legal status of a firm as a regular dealer or manufacturer within the meaning of the Walsh-Healey Act is for determination solely by the procuring agency, the

Small Business Administration (if a small business is involved) and the Secretary of Labor. 41 U.S.C. 35-45.

(10) Subcontractor Protests. The General Accounting Office will not consider subcontractor protests except where the subcontract is by or for the government.

(11) Judicial Proceedings. The General Accounting Office will not consider protests where the matter involved is the subject of litigation before a court of competent jurisdiction, unless the court requests a decision by the General Accounting Office. The General Accounting Office will not consider protests where the matter involved has been decided on the merits by a court of competent jurisdiction.

(g) A protest decision may not be delayed by the failure of a party to file a submission within the specified time limits. Consequently, the failure of any party or contracting agenty to comply with the prescribed time limits may result in resolution of the protest without consideration of the untimely submission.

§ 21.4 Withholding of award and suspension of contract performance.

Sections 3553 (c) and (d) of the Competition in Contracting Act of 1984, Pub. L. 98-369, set forth the following requirements regarding the withholding of award and suspension of contract performance when a protest is filed with the General Accounting Office. The requirements are included here for informational purposes.

(a) When the contracting agency receives notice of a protest from the General Accounting Office prior to award of a contract it may not award a contract under the protested procurement while the protest is pending unless the head of the procuring activity responsible for award of the contract determines in writing and reports to the General Accounting Office that urgent and compelling circumstances significantly affecting interests of the United States will not permit waiting for the General Accounting Office decision. This finding may be made only if the award is otherwise likely to occur within 30 days.

(b) When the contracting agency receives notice of a protest from the General Accounting Office after award of a contract, but within 10 days of the date of contract award, it shall immediately direct the contractor to cease contract performance and to suspend related activities that may result in additional obligations being incurred by the government under that contract while the protest is pending. The head of the procuring activity responsible for award of the contract may authorize contract performance notwithstanding the pending protest if he determines in writing and reports to the General Accounting Office that:

(1) Performance of the contract is in the government's best interest, or

(2) Urgent and compelling circumstances significantly affecting interests of the United States will not permit waiting for the General Accounting Office's decision.

§ 21.5 Conference.

(a) As conference on the merits of the protests may, at the sole discretion of the General Accounting Office, be held at the request of the protester, interested parties who have responded to the notice given under § 21.3(a), or the contracting agency. Requests for a conference should be made at the earliest possible time in the protest proceeding.

(b) Conferences will be held on a date set by the General Accounting Office no later than 5 days after receipt by the protester and interested parties of the agency report. All such interested parties shall be invited to attend. Ordinarily, only one conference will be held on a bid protest.

(c) If a conference is held, no separate comments under § 21.3(e) will be considered. The protester, all interested parties and the contracting agency may file comments on the conference and report as appropriate with the General Accounting Office, with copies furnished to the other parties, within 5 days of the date on which the conference was held.

(d) The General Accounting Office may request that a conference be held if at any time during the protest proceeding it decides that such a conference is needed to clarify material issues. If such a conference is held, the General Accounting Office shall make such adjustments in the submission deadlines as it determines to be fair to all parties.

(e) Failure of the protester to file comments, or to file a statement requesting that the case be decided on the existing record, or to request an extension under this section within the 5-day period set forth in paragraph (c) of this section will result in dismissal of the protest. The General Accounting Office may set a new date for the submission of comments under the circumstances set forth in § 21.3(e).

§ 21.6 Remedies.

(a) If the General Accounting Office determines that a solicitation, proposed award, or award does not comply with statute or regulation, it shall recommend that the contracting agency implement any combination of the following remedies which it deems appropriate under the circumstances:

(1) Refrain from exercising options under the contract;

(2) Terminate the contract;

(3) Recompete the contract;

(4) Issue a new solicitation;

(5) Award a contract consistent with statute and regulation; or

(6) Such other recommendations as the General Accounting Office determines necessary to promote compliance.

(b) In determining the appropriate recommendation, the General Accounting Office, shall, except as specified in paragraph (c) of this section, consider all the circumstances surrounding the procurement or proposed procurement including, but not limited to, the seriousness of the procurement deficiency, the degree of prejudice to other interested parties or to the integrity of the competitive procurement system, the good faith of the parties, the extent of performance, cost to the government, the urgency of the procurement and the impact of the recommendation on the contracting agency's mission.

(c) If the head of the procuring activity makes the finding referred to in § 21.4(b)(1) that performance of the contract notwithstanding a pending protest is in the government's best interest, the General Accounting Office shall make its recommendation under paragraph (a) of this section without regard to any cost or disruption from terminating, recompeting or reawarding the contract.

(d) If the General Accounting Office determines that a solicitation, proposed award, or award does not comply with statute or regulation it may declare the protester to be entitled to reasonable costs of:

(1) Filing and pursuing the protest, including attorney's fees; and

(2) Bid and proposal preparation.

(e) The General Accounting Office will allow the recovery of costs under paragraph (d)(1) of this section where the contracting agency has unreasonably excluded the protester from the procurement except where the General Accounting Office recommends pursuant to paragraph (a)(5) that the contract be awarded to the protester and the protester receives the award. The General Accounting Office will only allow the recovery of costs under paragraph (d)(2) of this section where the contracting agency has unreasonably excluded the protester from the procurement and where other remedies listed in paragraphs (a)(2)-(5) are not appropriate.

(f) If the General Accounting Office decides that the protester is entitled to the recovery of such costs, the protester and the contracting agency shall attempt to reach agreement on the amount of the costs. If the protester and the contracting agency cannot reach agreement within a reasonable time, the General Accounting Office will determine the amount.

§ 21.7 Time for decision by the General Accounting Office.

(a) The General Accounting Office shall issue a decision on a protest within 90 days from the date the protest is filed with it.

(b) In those protests for which the General Accounting Office invokes the express option under § 21.8, the General Accounting Office shall issue a decision within 45 calendar days from the date the protest is filed with it.

(c) Under exceptional circumstances the General Accounting Office may extend the deadlines in paragraph (a) of this section on a case-by-case basis by stating in writing the reasons that the specific circumstances of the protest require a longer period.

§ 21.8 Express option.

(a) At the request of the protester, the contracting agency or an interested party for an expeditious decision, the General Accounting Office will consider the feasibility of using an express option.

(b) The express option will be invoked solely at the discretion of the General Accounting Office only in those cases suitable for resolution within 45 calendar days.

(c) Requests for the express option must be in writing and received in the General Accounting Office no later than 3 days after the protest is filed. The General Accounting Office will determine within 2 days of receipt of the request whether to invoke the express option and will notify the contracting agency, protester and interested parties who have responded to the notice under § 21.3(a).

(d) When the express option is used the filing deadlines in § 21.3 and the provisions of § 21.5 shall not apply and:

(1) The contracting agency shall file a complete report with the General Accounting Office on the protest within 10 days from the date it receives notice from the General Accounting Office that the express option will be used and furnish copies of the report to the protester and interested parties who have responded to the notice under §21.3(a).

(2) Comments on the agency report shall be filed with the General Accounting Office within 5 days after receipt of the report with a copy furnished by the commenting party to the contracting agency and other participating interested parties.

(3) The General Accounting Office may arrange a conference to ascertain and clarify the material issues at any time deemed appropriate during the protest proceeding.

(4) The General Accounting Office shall issue its decision within 45 calendar days from the date the protest is filed with it.

§ 21.9 Effect of judicial proceedings.

(a) The General Accounting Office will dismiss any protest where the matter involved is the subject of litigation before a court of competent jurisdiction, unless the court requests a decision by the General Accounting Office. The General Accounting Office will dismiss any protest where the matter involved has been decided on the merits by a court of competent jurisdiction.

(b) Where the court requests a decision by the General Accounting Office, the times for filing the agency report (§ 21.3(c)), filing comments on the report (§ 21.3(e)), holding a conference and filing comments (§ 21.5), and issuing a decision (§ 21.7) may be changed if the court so orders.

§ 21.10 Signing and distribution of decisions.

Each bid protest decision shall be signed by the Comptroller General or a designee for that purpose. A copy of the decision shall be made available to all participating interested parties, the protester, the head of the contracting activity responsible for the protested procurement, the senior procurement executive of each federal agency involved, and any member of the public.

§ 21.11 Nonstatutory protests.

(a) The General Accounting Office may consider protests concerning sales by a federal agency or procurements by agencies of the government other than federal agencies as defined in § 21.0(b) or by the District of Columbia, if the agency involved has agreed in writing to have its protests decided by the General Accounting Office.

(b) All of the provisions of these Bid Protest Regulations shall apply to any nonstatutory protest decided by the General Accounting Office except for the provisions of § 21.6(d) pertaining to entitlement to reasonable costs of filing and pursuing the protest, including attorney's fees. Sections 3553 (c) and (d) of the Competition in Contracting Act of 1984, Pub. L. 98-369, pertaining to withholding of award and suspension of contract performance shall not apply.

§ 21.12 Request for reconsideration.

(a) Reconsideration of a decision of the General Accounting Office may be requested by the protester, any interested party who participated in the protest, and any federal agency involved in the protest. The General Accounting Office will not consider any request for reconsideration which does not contain a detailed statement of the factual and legal grounds upon which reversal or modification is deemed warranted, specifying any errors of law made or information not previously considered.

(b) Request for reconsideration of a decision of the General Accounting Office shall be filed, with copies to any federal agency and interested parties who participated in the protest, not later than 10 days after the basis for reconsideration is known or should have been known, whichever is earlier. The term "filed" as used in this section means receipt in the General Accounting Office.

(c) A request for reconsideration shall be subject to those bid protest regulations consistent with the need for prompt and fair resolution of the matter. The filing of a request for reconsideration will not invoke Section 3553 (c) or (d) of the Competition in Contracting Act of 1984, Pub. L. 98-369 relating to the withholding of award and the suspension of contract performance.

PART 22—PROCEDURES FOR DECISIONS ON APPROPRIATED FUND EXPENDITURES WHICH ARE OF MUTUAL CONCERN TO AGENCIES AND LABOR ORGANIZATIONS

Sec.
22.1 Purpose and scope.
22.2 Who may request a decision.
22.3 Contents of a request for a decision.
22.4 Service.
22.5 Request for an advisory opinion.
22.6 Time for issuance of decisions and advisory opinions.
22.7 Deference to grievance and arbitration procedures established pursuant to 5 U.S.C. Chapter 71.
22.8 Discretion to decline issuance of a decision.
22.9 Distribution of decisions.

AUTHORITY: 31 U.S.C. 711 and 3529.

SOURCE: 45 FR 55691, Aug. 21, 1980, unless otherwise noted. Redesignated at 45 FR 68374, Oct. 15, 1980.

§ 22.1 Purpose and scope.

This part sets forth the procedures which govern requests for decisions concerning the legality of appropriated fund expenditures on matters of mutual concern to Federal agencies and labor organizations participating in the labor-management program established pursuant to 5 U.S.C. Chapter 71, and other Federal sector labor-management programs. It gives labor organizations and Federal agencies equal access to GAO on any matter of mutual concern involving the expenditure of appropriated funds, and extends the right to request an advisory opinion on such matters to arbitrators and other neutral parties. It also provides guidance as to when GAO will defer to procedures established pursuant to 5 U.S.C. Chapter 71.

§ 22.2 Who may request a decision.

Heads of Federal agencies and departments (or their designees), heads of labor organizations representing Federal employees (or their designees), and authorized certifying or disbursing officers may request a decision under this part.

§ 22.3 Contents of a request for a decision.

A request for a decision shall be in writing, dated, signed by the requester, addressed to the Comptroller General of the United States, General Accounting Office, Washington, D.C. 20548, and contain as applicable:

(a) The name and address of the party requesting the decision;

(b) A statement of the question to be decided, a presentation of all relevant facts, and a statement of the party's argument;

(c) Copies of all pertinent records and support documents;

(d) Notice as to whether the matter is subject to a negotiated grievance procedure, and whether a grievance has been filed or any other procedure has been invoked to adjudicate the same or a substantially similar matter before the Federal Labor Relations Authority or other administrative body or court; and

(e) A power of attorney or statement of authority to represent if required by 4 CFR Part 11.

[45 FR 55691, Aug. 21, 1980. Redesignated at 45 FR 68374, Oct. 15, 1980, and amended at 47 FR 56980, Dec. 22, 1982]

§ 22.4 Service.

(a) Any person requesting a decision under this part is responsible for promptly forwarding a copy of the request and supporting documents to all known interested parties. Service shall be made by registered or certified mail or in person. When service is by mail, the date of service shall be the date when the document served is deposited in the United States mail.

(b) A signed and dated statement of service shall be submitted along with the request and indicate the names of the parties and persons served, their addresses, the date of service, the nature of the document served, and the manner in which service was made.

(c) Any party served or any other person may submit a written response to the request for a decision to the Comptroller General of the United States, General Accounting Office, Washington, D.C. 20548. Any such response should be submitted within 20 calendar days after the date of service of the request in order to ensure that it will be considered. Copies of written responses shall be promptly forwarded to all know interested parties in the manner prescribed in paragraphs (a) and (b) of this section.

§ 22.5 Request for an advisory opinion.

(a) Arbitrators and other neutral parties authorized to administer 5 U.S.C. Chapter 71 may request an advisory opinion on any matter involving the expenditure of appropriated funds which is of mutual concern to Federal agencies and labor organizations. A request for an advisory opinion shall be in writing, dated, signed by the requester, addressed to the General Counsel, U.S. General Accounting Office, Washington D.C. 20548, and contain all of the information referred to in § 22.3 (a) through (d). Consistent with § 22.8, the General Counsel retains the discretion to decline to issue an advisory opinion.

(b) Service of a request for an advisory opinion on the parties to the dispute or on other interested parties is discretionary with the requesting party. If service is made, it shall be in a manner consistent with § 22.4 (a) and (b), except that where the persons served have been previously provided with copies of records and support documents, the requester may instead serve them with a listing of the documents submitted to GAO.

(c) Any party served with a copy of a request for an advisory opinion may submit written comments on the request to the General Counsel, U.S. General Accounting Office, Washington, D.C. 20548. Copies of such comments shall be promptly served on all known interested parties. Comments should be submitted within 20 calendar days after the date of service of the request in order to ensure consideration by the General Counsel.

(d) A copy of the advisory opinion of the General Counsel will be forwarded to the requester and to all persons who have been served with a copy of the request.

§ 22.6 Time for issuance of decisions and advisory opinions.

Decisions and advisory opinions under this part will be issued as expeditiously as possible, normally within 60 calendar days after the expiration of the 20 day period for filing responses pursuant to § 22.4(c) or § 22.5(b). Where a delay is anticipated, interested parties will be notified and provided with a tentative date for issuance of the decision or advisory opinion.

§ 22.7 Deference to grievance and arbitration procedures established pursuant to 5 U.S.C. Chapter 71.

(a) *Final and binding arbitration awards.* Payments made pursuant to an arbitration award which is final and binding under 5 U.S.C. 7122 (a) or (b) will be considered conclusive on

GAO in its settlement of the accounts involved, and the Comptroller General will not review or comment on the merits of such an award. However, payments made pursuant to such an award do not constitute precedent for payment in other instances not covered by the award.

(b) *Matters subject to a grievance procedure.* The Comptroller General will not issue a decision or comment on the merits of a matter which is subject to a negotiated grievance procedure authorized by 5 U.S.C. 7121, except upon the request of an authorized certifying or disbursing officer, or the joint request of an agency and labor organization. Requests will be considered joint for purposes of this subsection when the other party has been served pursuant to § 22.4 and has not objected to submission of the matter to GAO.

(c) *Claims against the United States.* Except as provided in paragraph (a) of this section, nothing in this section restricts or limits an individual's right to have a claim against the United States adjudicated pursuant to Part 31 of Title 4, Code of Federal Regulations.

§ 22.8 Discretion to decline issuance of a decision.

The Comptroller General will not issue a decision on (a) any matter which the Comptroller General finds is more properly within the jurisdiction of the Federal Labor Relations Authority or other administrative body or court of competent jurisdiction, or (b) on a matter which the Comptroller General finds is unduly speculative or otherwise not appropriate for decision.

§ 22.9 Distribution of decisions.

(a) A copy of a decision of the Comptroller General will be forwarded to the requester and to all other interested parties of record.

(b) Any person interested in receiving copies of decisions issued under this part may request to be placed on the distribution list maintained for that purpose. Requests should be directed to the Chief, Legal Information and Reference Services, U.S. General Accounting Office, Washington, D.C. 20548.

PART 27—GENERAL ACCOUNTING OFFICE PERSONNEL APPEALS BOARD—ORGANIZATION

Sec.

27.1 The Board.
27.2 The Chair.
27.3 The General Counsel.

AUTHORITY: 31 U.S.C. 753.

SOURCE: 46 FR 35478, July 9, 1981, unless otherwise noted.

§ 27.1 The Board.

The General Accounting Office Personnel Appeals Board, hereinafter the Board, is composed of five members appointed by the Comptroller General, in accordance with the provisions of 31 U.S.C. 751. The Board may designate a panel of its members or an individual Board member to take any action within the scope of the Board's authority, subject to later reconsideration by the Board.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 27.2 The Chair.

The members of the Board shall select from among its membership a chairperson, hereinafter the Chair, who shall serve as the chief executive and administrative officer of the Board.

§ 27.3 The General Counsel.

The Comptroller General shall appoint the individual selected by the Chair to serve as the General Counsel of the Board. The General Counsel, at the request of the Board or of any member of the Board, shall investigate matters under the jurisdiction of the Board, and otherwise assist the Board in carrying out its functions, unless to do so would create a conflict of interest for the General Counsel.

PART 28—GENERAL ACCOUNTING OFFICE PERSONNEL APPEALS BOARD—PROCEDURES

Subpart A—Purpose and General Definitions

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Sec.

Subpart H—Appeals by Members of the Senior Executive Service

28.111 Personnel actions involving SES members.
28.113 Performance based actions.

Subpart I—Ex Parte Communications

28.117 Policy.
28.119 Explanation and definitions.
28.121 Prohibited communications.
28.123 Reporting of communications.
28.125 Sanctions.

AUTHORITY: 31 U.S.C. 753.

SOURCE: 46 FR 35478, July 9, 1981, unless otherwise noted.

Subpart A—Purpose and General Definitions

§ 28.1 Purpose and scope.

(a) The purpose of these rules is to establish the procedures to be followed:

(1) By the GAO, in its dealings with the Board;

(2) By employees of the GAO or applicants for employment by the GAO, or by groups or organizations claiming to be affected adversely by the operations of the GAO personnel system;

(3) By employees or organizations petitioning for protection of rights or extension of benefits granted to them under Subchapters III and IV of Chapter 7 of Title 31, U.S.C.; and

(4) By the Board, in carrying out its responsibilities under Subchapters III and IV of Chapter 7 of Title 31, U.S.C.

(b) The scope of the Board's operations encompasses the investigation and, where necessary, adjudication of cases arising under 31 U.S.C. 753. In addition, the Board has authority for oversight of the equal employment opportunity program at GAO. This includes the review of policies and evaluation of operations as they relate to EEO objectives and, where necessary, the ordering of corrective action for violations of or inconsistencies with equal opportunity laws in GAO.

(c) The intent of Subchapters III and IV of Chapter 7 of Title 31, U.S.C. is to provide the GAO independence in administering its labor and employee relations function intended by Subchapters III and IV of Chapter 7 of

Title 31, U.S.C., while ensuring that "GAO employees are entitled to the same rights and protections as employees in the executive branch." H.R. Rep. No. 96-494, 15 (1980). Such a broad scope of authority would normally require the promulgation of rules and regulations, in respect to the GAO, as extensive as those of all the agencies covering the relevant activities of the entire executive branch. To do so for but one agency, however, seems to the Board to be unnecessarily burdensome to all concerned. Instead, these regulations are designed to establish general guidelines which meet the immediate purpose of providing to all parties early and clear access to the Board.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.3 General definitions.

In this part—

(a) "Board" means the General Accounting Office Personnel Appeals Board as established by 31 U.S.C. 751.

(b) "Comptroller General" means the Comptroller General of the United States.

(c) "Days" means calendar days.

(d) "GAO" means the General Accounting Office.

(e) "General Counsel" means the General Counsel of the General Accounting Office Personnel Appeals Board, as provided for under 31 U.S.C. 752.

(f) "Hearing Officer" means any individual designated by the Board to preside over a hearing conducted on matters within its jurisdiction. A Hearing Officer may be a member of the Board, an employee of the Board, or any individual qualified by experience or training to conduct a hearing.

(g) "Person" means an employee or applicant for employment, a labor organization or the GAO.

(h) "Petition" means any request filed with the Board for action to be taken on matters within the jurisdiction of the Board, under the provisions of Subchapters III and IV of Chapter 7 of Title 31, U.S.C.

(i) "Petitioner" means any person filing a petition for Board consideration.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982; 48 FR 29665, June 28, 1983]

Subpart B—Procedures

§ 28.5 Informal procedural advice.

(a) Petitioners or prospective petitioners may seek informal advice on all aspects of the Board's procedures by contacting the General Counsel.

(b) Informal procedural advice will be supplied within the limits of available time and staff.

§ 28.7 Procedures—general.

The procedures described in this subpart are generally applicable to the processing of all matters presented for consideration by the Board. Where special procedures are to be followed, they will be prescribed in those subsequent subparts to which they are particularly applicable.

§ 28.9 Notice of appeal rights.

The GAO shall be responsible for insuring that employees are regularly advised of their appeal rights to the Board and that employees, who are the object of an adverse action, are, at the time of the action, adequately advised of their appeal rights to the Board.

§ 28.11 Filing a petition.

(a) *Who may file.* Any GAO employee or applicant for employment claiming to be affected adversely by GAO action or inaction which is within the Board's jurisdiction under Subchapters III and IV of Chapter 7 of Title 31, U.S.C.

(b) *When to file.* (1) Petitions for review of adverse actions based on conduct or performance must be filed within 20 days after the effective date of the action.

(2) Petitions for review of other personnel actions must be filed within 20 calendar days after the effective date of the action or 20 calendar days after the petitioner knew or should have known of the action.

(3) Petitions for review of adverse actions (paragraph (b)(1) of this section) or other personnel actions (paragraph (b)(2) of this section) that also

raise an allegation of prohibited discrimination must be filed in accordance with paragraph (b)(4) of this section.

(4) Petitions for review of discrimination complaints may be filed any time after 80 days have passed since the filing of a formal complaint of discrimination with GAO, except that, when GAO has issued a final agency decision, the petition for review must be filed within 20 calendar days from receipt by the petitioner of the final agency decision.

(5) Petitions for review of continuing violations may be filed at any time.

(6) The Board may waive the time limits in these rules for good cause shown.

(c) *How to file.* Petitions may be filed with the Board in person at the Office of the Board (GAO Building, Room 4057, Washington, D.C.) or by certified mail addressed to the General Counsel, GAO Personnel Appeals Board, Room 4057, Washington, D.C. 20548, or to the General Counsel, Personnel Appeals Board, P.O. Box 2496, Washington, D.C. 20013. When filed by mail, the post-mark shall be the date of filing for all submissions to the Board.

(d) *What to file.* The petitioner should include in any petition for Board action the following information:

(1) Name of the petitioner or a clear description of the group or class of persons on whose behalf the petition is being filed;

(2) The names and titles of persons, if any, responsible for actions the petitioner wishes to have the Board review;

(3) The actions being complained about, including dates, reasons given, and internal appeals taken;

(4) Petitioner's reasons for believing the actions to be improper;

(5) Remedies sought by the petitioner;

(6) Name and address of the representative, if any, who will act for the petitioner in any further stages of the matter;

(7) Copies of all relevant documentation;

(8) Signature of the petitioner or petitioner's representative.

(e) *Service on respondent.* Upon receipt of a petition for review, the General Counsel shall serve a copy on the respondent. The respondent shall have 20 days in which to reply.

(f) *Class actions.* One or more employees may file an appeal as representatives of a class of employees in any matter within the Board's jurisdiction other than prohibited discrimination (see § 28.45 for EEO class actions). The hearing officer shall hear the case as a class action if he/she finds a class action will be the most efficient and fair way to adjudicate the appeal and will adequately protect the interests of all the parties. For the purpose of determining whether it is appropriate to treat an appeal as a class action, the hearing officer will be guided, but not controlled by, the applicable provisions of the Federal Rules of Civil Procedure.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.13 Amendments to petitions.

The Board at its discretion may allow amendments to a petition as long as all persons who are parties to the proceeding have adequate notice to prepare for the new allegations.

§ 28.15 GAO response.

Within 20 days after receiving a copy of a petition filed in accordance with § 28.11, where GAO is a party from whom the petitioner seeks relief, the GAO shall file a response containing at least the following:

(a) A complete statement of the GAO position with respect to each of the issues raised by the petitioner, including admissions, denials or explanations of each allegation made in the petition.

(b) All documents or true copies thereof contained on the GAO records regarding the matter.

(c) Designation of, and signature by, the GAO representative authorized to act for GAO in the matter.

§ 28.17 General Counsel procedures.

(a) All petitions filed in accordance with § 28.11 will be received by the General Counsel for the Board. The General Counsel will investigate the matter, refine the issues where appropriate, and attempt settlement of all matters at issue.

(b) The General Counsel may issue subpoenas requiring the attendance and testimony of witnesses and the production of documentary or other evidence and order the taking of depositions and order responses to written interrogatories in connection with an investigation under these Rules by the General Counsel. Employees of GAO who are required by the General Counsel to participate in any investigation under these Rules shall be on official time.

(c) Following the investigation, the General Counsel shall provide the petitioner with a Right to Appeal Letter. Accompanying this letter will be a Report and Recommendations of the General Counsel advising the petitioner of the results of the investigation. This Report and Recommendations of the General Counsel is not subject to discovery and may not be introduced into evidence before the Board.

(d) If, following the investigation, the General Counsel determines that there is not reasonable evidence to believe that the petitioner's rights under Subchapters III and IV of Chapter 7 of Title 31, U.S.C. have been violated, then the General Counsel shall not represent petitioner. If the General Counsel determines that there is reasonable evidence to believe that the petitioner's rights under Subchapters III and IV of Chapter 7 of Title 31, U.S.C. have been violated, then the General Counsel shall represent petitioner unless the petitioner elects not to be represented by the General Counsel. Such petitioner may represent himself/herself or obtain other legal counsel.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.19 Board procedures—pre-hearing.

(a) Where the procedures for the General Counsel's investigation have been completed and the petitioner petitions the Board for relief, the Board shall order a hearing on its own motion or at the request of either party. Absent a request for a hearing, the Board may issue a Decision and Order based upon the written submissions of the parties and, where it deems necessary, on oral argument called for the purpose of eliciting further views.

(b) All motions of the parties shall be filed with the Hearing Officer assigned by the Board after receipt of the petition, and copies shall be served simultaneously upon the other parties to the petition. Responses in opposition to such motions must be filed with the Hearing Officer and served simultaneously upon the other parties to the petition within 20 days of receipt of the motion, unless the Hearing Officer requires a shorter response time. A certificate of service will be filed with all pleadings showing service by mail or personal delivery of the pleadings to the other parties. Additional responsive pleadings may be filed only with the approval of the Hearing Officer.

(c) Requests for discovery may be served upon a party following the filing of a Petition for Review. Objections to any or all portions of a request must be served within 10 days of receipt of the request. Otherwise, compliance with the request shall be made within 20 days of receipt. If the parties are unable to agree as to the scope of discovery, the Hearing Officer shall, upon the filing of a motion to compel, rule on such questions, having in mind the need to provide a full and fair consideration of the relevant and material facts of the case. Appropriate safeguards for the confidentiality of information discovered may be imposed by the Hearing Officer.

(d) Where the General Counsel under § 28.17(a) transmits a settlement, which has been agreed to by the parties, the settlement agreement shall be the final disposition of the case.

[46 FR 35478, July 9, 1981, as amended at 48 FR 29665, June 28, 1983]

§ 28.21 Board procedures—formal hearings.

(a) Where two or more parties have filed petitions containing identical or similar issues, the Board may, following appropriate notice to the parties and opportunity for comment by the

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parties, consolidate such petitions for hearing purposes.

(b) Where a petitioner has filed two or more petitions, the Board may, following appropriate notice to the parties and opportunity for comment by the parties, join these petitions for purposes of conducting the hearing.

(c) A formal hearing on a petition may be conducted:

(1) Before the Board as a whole, in which case the Chair shall preside;

(2) Before one of its members chosen by the Board to be the Hearing Officer;

(3) Before a panel of two or more Board members chosen by the Board, one of whom shall preside;

(4) Before a qualified Hearing Officer chosen by the Board for that purpose.

(d) The Board shall issue a notice to all parties specifying the date, time and place of the scheduled hearing. In no case shall the hearing be held earlier than 15 days after the notice is issued, unless all parties agree to an earlier date.

(e) Upon request by the Board, the GAO shall provide appropriate space to hold the hearing.

(f) The Hearing Record shall be prepared and maintained under the supervision of the Hearing Officer. It shall include exhibits, motions, and other material submitted by the parties and accepted by the Hearing Officer. It may also, at the election of the Hearing Officer, include a transcript of the hearing. This Record shall constitute the sole official record of the proceeding. Copies of all or portions of the Record shall be provided to the petitioner and the respondent upon request; other parties may be furnished a copy, at their request and at their own expense, or they may examine a copy at a time and place set by the Board.

(g) Generally, hearings shall be closed to the public unless the petitioner requests the Hearing Officer to order the hearing or part of the hearing to be open. However, the Hearing Officer may, for good cause shown, close any or all portions of the hearing, over the petitioner's objections, stating the reason therefor on the record.

(h) Although the rules of evidence shall not apply, the Hearing Officer shall conduct the hearing so as to ensure that all relevant and material facts are placed into the record and all parties are given full opportunity to present their evidence on the issues.

(i) The Hearing Officer shall conduct the hearing in a manner designed best to achieve a balance of fairness, justice and equity in terms of the objectives of Subchapters III and IV of Chapter 7 of Title 31, U.S.C. and the proper interests of the parties; he/she shall have the authority needed to function effectively, including, but not restricted to authorizing the taking of depositions, ruling on admissibility of evidence, issuing subpoenas, requiring briefs, and administering oaths.

(j) The Hearing Officer shall rule on all questions of procedure and conduct raised at the hearing following appropriate administrative procedures consistent with 5 U.S.C. 7701 and 7702. Objections to rulings of the Hearing Officer, with reasons therefor, shall be part of the record; however, the hearing shall proceed as ordered by the Hearing Officer.

(k) Upon application to the Hearing Officer, any party affected by matters at issue in any petition may be given, at the discretion of the Hearing Officer, the status of an intervenor in all formal proceedings relating to the petition. As such, any intervenor shall have the right to participate in the hearing and to be notified, as is the petitioner, of all Board actions respecting the processing of the case. However, intervenors shall pay any costs related to their participation in the processing of the petition.

(l) The costs involved in the appearance of witnesses in any Board hearing shall be allocated as follows:

(1) Persons employed by the GAO shall, upon request by the Hearing Officer to GAO, be made available to participate in the hearing and shall be in official duty status for this purpose. They shall not receive witness fees.

(2) Employees of other Federal agencies called to testify at a Board hearing shall, at the request of the Hearing Officer and with the approval of the employing agency, be in official duty status during any period of ab-

sence from normal duties caused by their testimony, and shall not receive witness fees. In the event that the employing agency refuses the request to release the employee-witness in an official duty status, the employee-witness may be paid a witness fee in accordance with paragraphs (l)(3) and (m) of this section.

(3) The fees and expenses of other persons called to testify at a Board hearing shall, in the first instance, be paid by the party requesting their appearance, subject to a subsequent decision otherwise in accordance with paragraph (m) of this section.

(m) Within 20 days after receipt of a notice of final decision by the Board, the petitioner may submit a request for the award of reasonable attorney's fees and costs. GAO may file a response to the request within 20 days after its receipt. Motions of the parties shall be filed in accordance with § 28.19(b) of these regulations. Rulings of the Board on attorney's fees and costs shall be consistent with the standards set forth at 5 U.S.C. 7701(g). The Board's decision on attorney's fees and costs shall be a final decision, in accordance with § 28.27.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982; 48 FR 29666, June 28, 1983]

§ 28.23 Burden and degree of proof.

(a) In appealable actions, as defined by 5 U.S.C. 7701(a), agency action must be sustained by the Board if:

(1) It is a performance-based action and is supported by substantial evidence; or

(2) It is brought under any other provision of law, rule or regulation as defined by 5 U.S.C. 7701(a) and is supported by a preponderance of evidence.

(b) Notwithstanding paragraph (a) of this section, the agency's decision may not be sustained if the petitioner—

(1) Shows harmful error in the application of the agency's procedures in arriving at such decision;

(2) Shows that the decision was based on any prohibited personnel practice described in 4 CFR 2.5; or

(3) Shows that the decision was not in accordance with law.

(c) In any other appeal to the Board, the petitioner shall have the responsibility of presenting the evidence in support of the appeal and shall have the burden of proving the allegations of the appeal by a preponderance of the evidence.

§ 28.25 Board procedures—decisions and orders.

(a) Where a Hearing Officer who is not a Board member conducts a hearing, the Hearing Officer shall transmit to the parties and the Board a Report of Findings of Fact and Recommendations. Based upon this Report, a member or panel of members of the Board shall issue a decision. The decision shall contain the date upon which the decision will become final, which will be at least 30 days from issuance. The decision shall become final on that date unless, prior to that date, a party files a motion to reopen and reconsider or unless the Board reopens on its own motion.

(b) Where a Board member or panel of Board members hears a case, a decision shall be issued to the Board and to the parties. The decision shall contain the date upon which the decision will become final, which will be at least 30 days from issuance. The decision shall be final on that date unless, prior to that date, a party files a motion to reopen and reconsider or unless the Board reopens on its own motion.

(c) A motion to reopen and reconsider a decision may be filed with the Board in person or by certified mail. The motion to reopen and reconsider shall set forth objections to the decision, with references to applicable laws or regulations, and with specific reference to the Record. The Board shall serve a copy of the motion to reopen and reconsider on the other parties and allow 20 days for response to the motion. The Board may grant a motion to reopen and reconsider when it is established that:

(1) New and material evidence is available that, despite due diligence, was not available when the record was closed; or

(2) The decision of the Hearing Officer is based on an erroneous interpretation of statute or regulation.

(d) If the Board reopens a case, the subsequent decision of the Board shall be final.

(e) Where the full Board initially hears a case, the subsequent decision shall be final and appealable under § 28.27.

(f) A person required to take any action under the terms of a Board decision or order shall carry out its terms promptly, and shall, within 30 days after the decision or order becomes final, provide the Board with compliance report specifying:

(1) The manner in which the provisions of the decision or order have been compiled with;

(2) The reasons any provisions have not yet been fully complied with; and

(3) The steps being taken to ensure full compliance.

A copy of the report shall be served on all parties to the proceeding.

(g) The Administrative Officer of the Board shall take all necessary action to ascertain whether the final decision of the Board is being complied with. If the Administrative Officer finds non-compliance, he/she shall undertake efforts to obtain compliance. If the Administrative Officer is unable to obtain satisfactory agency compliance with the final order, he/she shall report to the Board.

(h) Any person may petition the Board for enforcement of a final decision. The petition shall specifically set forth the reasons why the petitioner believes there is non-compliance.

(i) Upon receipt of a non-compliance report from its Administrative Officer or of a petition for enforcement of a final decision, the Board may issue a notice to any person to show cause why there was non-compliance.

(j) Following a show cause proceeding, the Board may seek judicial enforcement of its decision or order.

[46 FR 35478, July 9, 1981, as amended at 48 FR 29666, June 28, 1983]

§ 28.27 Board procedures—judicial review.

(a) *Appeals other than discrimination complaints.* A final decision by the Board under subsections 4(h) (1), (2), (3), (6), and (7) of the Act may be appealed to the United States Court of Appeals for the Circuit in which the petitioner resides or to the United States Court of Appeals for the District of Columbia within 30 days after the date the petitioner receives notice from the Board of the final decision.

(b) *Judicial review of discrimination complaints.* The provisions for review of discrimination complaints are provided in § 28.51.

(c) The Board may designate the General Counsel or any other qualified individual to represent it in any judicial appeals from its Decisions taken in accordance with 31 U.S.C. 755.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982; 48 FR 29666, June 28, 1983]

Subpart C—Oversight Procedures

§ 28.31 General.

Section 732(f) of Title 31, U.S.C. provides that, with respect to employees and applicants for employment in the GAO, the authority granted in the legislation under 31 U.S.C. 732(f)(2), which involves oversight of the EEO program and appeals relating to EEO matters, shall be exercised by the Board. The EEO appeals procedures are delineated in Subpart D of these regulations. This Subpart specifies the oversight procedures required to ensure that the goals of the legislation will be attained through the development and administration of personnel procedures as well as by dealing with specific cases involving allegations of illegal practices.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.33 Oversight of GAO EEO program.

(a) In order to carry out the purpose of this subpart, the Board may require from GAO the following:

(1) Such plans, procedures and regulations as GAO may develop in order to carry out the purposes enumerated in § 28.41;

(2) Reports regarding its efforts to publicize to its employees the procedures to be followed for receiving advice and for filing complaints re-

garding the enforcement of laws prohibiting discrimination in employment;

(3) Quarterly statistical reports of pre-complaint counseling and of pending complaints, in a manner prescribed by the Board;

(4) An annual report on its equal employment opportunity affirmative action program and its Federal Equal Employment Opportunity Recruitment Program; and

(5) Any other information requested by the Board regarding equal employment opportunity within the GAO that may be required by the Board in the time frame and format established by the Board after consultation with the Comptroller General or his/her designee.

(b) The Board shall review and evaluate the regulations, procedures and practices of the GAO, including the information filed with it in accordance with § 28.33(a), and shall:

(1) Require the GAO to make any changes the Board determines are needed due to violations of or inconsistencies with Subchapters III and IV of Chapter 7 of Title 31, U.S.C. or equal employment opportunity laws, and

(2) Report to the Congress on the overall progress being made in effectuating the purposes of Subchapters III and IV of Chapter 7 of Title 31, U.S.C.

(c) The Board delegates to the General Counsel responsibility for conducting investigations, in the absence of a formal allegation, for the purpose of determining whether there are reasonable grounds to believe that a violation of 31 U.S.C. 732(f)(2) exists. For these purposes the provisions of § 28.17(b) shall apply.

(d) If the General Counsel determines that disciplinary action should be taken against an employee after any investigation under this section, the General Counsel shall prepare a written complaint against the employee containing his/her determination, together with a statement of the supporting facts, and present the complaint and the statement to the employee and the Board for processing in accordance with Subpart G.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

Subpart D—Special Procedures—Equal Employment Opportunity Cases

§ 28.41 Purpose and scope.

The procedures in this subpart relate to complaints filed against any GAO policies or specific actions which petitioners claim are in violation of:

(a) Section 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000e-16), prohibiting discrimination based on race, color, religion, sex or national origin;

(b) Sections 12 and 15 of the Age Discrimination in Employment Act of 1967 (29 U.S.C. 631, 633a) prohibiting discrimination on account of age;

(c) Section 6(d) of the Fair Labor Standards Act of 1938 (29 U.S.C. 206(d)), prohibiting discrimination in wages on the basis of sex;

(d) Sections 501 and 505 of the Rehabilitation Act of 1973 (29 U.S.C. 791, 794a) prohibiting discrimination on the basis of handicap; or

(e) "[A]ny other law prohibiting discrimination in Federal employment on the basis of race, color, religion, age, sex, national origin, political affiliation, marital status or handicapping condition. . . ." 31 U.S.C. 732(f)(2).

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.43 Applicability of general procedures.

Except where a different procedure is provided for in this subpart, the procedures to be followed by all parties in cases arising under this subpart shall be the General Procedures as prescribed in Subpart B of these regulations.

§ 28.45 Class action appeals.

(a) A petition alleging prohibited discrimination on behalf of a class of GAO employees or applicants for employment must first be filed with GAO in accordance with GAO Order 2713.2.

(b) A Petition for Review of GAO's disposition of any EEO class complaint may be submitted for consideration when:

(1) GAO issues a determination rejecting or cancelling the class complaint;

(2) GAO issues a determination accepting the class action, but with modifications that are not satisfactory to the agent of the Class;

(3) A period of more than 180 days has elapsed since the formal class complaint was filed and the GAO has not issued a final decision; or

(4) The complaint has been resolved by a GAO decision that, in whole or in part, has not satisfied the agent for the class.

(c) The parties shall not have a right to a hearing in class actions under this section. Upon a showing of good cause as to why an evidentiary hearing is necessary, the Board may order such a hearing. Alternatively, the Board may, after a review of the administrative record and on its own motion, order a hearing for the purpose of gathering additional evidence. If no hearing is ordered, the Board's decision shall be based upon a review of the administrative record developed in the GAO class complaint process.

(d) In determining whether it is appropriate to treat an appeal as a class action, the Board will be guided, but not controlled by, the applicable provisions of the Federal Rules of Civil Procedure.

§ 28.47 Petitions to the Board.

(a) The purposes and policies of the various statutes that prohibit discrimination can best be achieved through conscientious use by employees and management of the agency complaint process. To this end, the Board and the General Counsel will require full utilization by the parties of the EEO complaint process within GAO, except when the General Counsel elects to proceed in accordance with § 28.107. Therefore, if an employee is alleging EEO related improprieties, the employee must generally pursue the agency EEO complaint process before petitioning the Board.

(b) A petition for review of GAO's disposition of any EEO complaint may be submitted for consideration of the Board when:

(1) The complaint or a portion thereof has been rejected by the GAO;

(2) A period of more than 80 days has elapsed since the complaint was filed, and the GAO has not issued a final decision; or

(3) The complaint has been resolved by a GAO decision which, in whole or in part, has not satisfied the complainant.

(c) Where a petitioner wishes to file a combination of claims, only a portion of which involve discrimination, the petitioner must first file a complaint in the agency EEO complaint process. Where a complaint filed in the agency EEO complaint process relates to non-EEO issues that are within the Board's jurisidcation in addition to EEO-related allegations, the subsequent petition to the Board under paragraph (b) of this section shall be considered a timely appeal of the non-EEO issues.

(d) A petition filed with the General Counsel under the provisions of this subpart shall state the issue briefly, and shall spell out clearly the reason the petitioner believes the action of the GAO to be contrary to the law.

(e) The petitioner shall file the petition with the General Counsel in accordance with § 28.11. The General Counsel shall serve the GAO with a copy of the petition and request that the GAO provide within 10 days of receipt any file or portion thereof that may exist.

§ 28.49 Processing petitions.

(a) In addition to submitting the complaint file under § 28.47(e), GAO may file a response to the petition in accordance with § 28.15.

(b) The provisions of §§ 28.17 through 28.25, inclusive, shall govern the Boards's procedures in processing petitions filed under this subpart.

(c) Remedial action provided in Board orders in these cases may include:

(1) Provision for offers of employment, re-employment or promotion, with or without back-pay, when the Board decides such action is required to make whole the individual found to have been discriminated against.

(2) Notification to all GAO employees of the action ordered to be taken to expunge the effect of the discrimination;

(3) Correction of GAO personnel records, as necessary, to reflect the purpose of the Board order; and,

(4) Any other action the Board believes is proper to correct the effect of the discrimination found to have occurred.

§ 28.51 Civil action—discrimination complaints.

(a) An employee or applicant alleging violations of 42 U.S.C. 2000e-16 (Title VII of the Civil Rights Act of 1964, as amended) may file suit in Federal District Court after 120 days from filing a complaint with GAO if there is no final decision on that complaint or within 30 days of receipt of notice of final action taken by GAO.

(b) An employee or applicant alleging violations of 42 U.S.C. 2000e-16 (Title VII of the Civil Rights Act of 1964, as amended) may file suit in Federal District Court after 120 days from filing an appeal with the Board if there is no final decision on that discrimination appeal or within 30 days of receipt of notice of final action by the Board.

(c) Employees or applicants for employment alleging discrimination based upon a handicapping condition (29 U.S.C. 791, 794a—Rehabilitation Act), or age discrimination (29 U.S.C. 631, 633a—Age Discrimination in Employment Act), or salary inequity due to sex (29 U.S.C. 206d—Equal Pay Act provisions of the Fair Labor Standards Act) need not exhaust administrative appeals to GAO or to the Board before filing suit in the Federal District Court.

[46 FR 35478, July 9, 1981, as amended at 48 FR 29666, June 28, 1983]

Subpart E—Special Procedures—Representation Proceedings

§ 28.61 Purpose.

The procedures in this subpart relate to the Board's duty under 31 U.S.C. 753(a) (4) and (5) to determine appropriate units of GAO employees for collective bargaining, to conduct elections in order to determine whether the employees in any such units wish to select a labor organization to represent them in collective bargaining, and, thereafter, to certify labor organizations so selected as the designated exclusive bargaining representative. They are referred to in these regulations as "representation proceedings".

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.63 Scope.

The Board shall consider, decide and order corrective action (as appropriate) in cases arising from determinations of appropriate units of employees for collective bargaining and cases arising from elections and certifications of collective bargaining representatives. Board decisions in these matters will be made with due regard for relevant provisions of GAO Orders and with the objective of insuring that the GAO labor relations program is consistent with Chapter 71 of Title 5, United States Code, which prescribes the standards for the labor relations program in the executive branch.

§ 28.65 Who may file petitions.

(a) Representation petitions may be filed by:

(1) A labor organization which wishes to be designated as the exclusive representative for collective bargaining by the GAO employees in an appropriate unit, or by a labor organization which desires to replace another currently having that status;

(2) An employee or a group of employees (or an individual on his/her/their behalf) desiring a new election to determine whether a labor organization has ceased to represent a majority of employees in a unit;

(3) The GAO if it has a good faith reason to doubt the continued desire of a group of its employees to be represented by a labor organization which is currently the exclusive representative of the employees in an appropriate unit;

(4) The GAO or a labor organization currently recognized as an exclusive representative, desiring the Board to clarify an earlier unit determination or certification;

(5) Any person seeking clarification of, or an amendment to, a certification

then in effect or any other matter relating to representation.

(b) Notwithstanding the provisions of paragraph (a) of this section, no petition may be filed which seeks representation rights for employees in a unit—

(1) Where an election has been held within the previous 12 calendar months and in such election a majority of the employees voting chose a labor organization for certification as the unit's exclusive representative or

(2) Where an existing collective bargaining agreement is in effect, unless the petition for exclusive recognition is filed not more than 105 days and not less than 60 days before the expiration of the collective bargaining agreement or

(3) Where an excellent collective bargaining agreement is in effect for more than three years, then the petition for recognition shall be filed not more than 105 days and not less than 60 days before the third anniversary and each subsequent anniversary of the collective bargaining agreement.

[46 FR 35478, July 9, 1981, as amended at 48 FR 29666, June 28, 1983]

§ 28.67 Contents of representation petitions.

(a) The contents of representation petitions filed under § 28.65(a)(1) shall consist of:

(1) A detailed identification of the unit of employees to which the petition applies, and their geographical location within the GAO, the classifications of employees to be included and excluded, and the number of employees involved.

(2) Names, addresses and officers of any other labor organizations known by the petitioner to be interested in representing employees covered by the petition, including a labor organization which is party to a current collective bargaining agreement covering any employees in the unit;

(3) Name, address, affiliation, if any, and telephone number of the petitioning organization;

(4) A copy of the constitution and bylaws of the organization, together with a statement that these documents, as well as a roster of the organization's officers and representatives and a statement of the objectives, have also been supplied to the GAO.

(5) A declaration by the signer of the petition, under penalties of the Criminal Code (18 U.S.C. 1101), that the petition's contents are true and correct, to the best of his/her knowledge and belief;

(6) The signature of the representative of the petitioner, including title and telephone number; and

(7) Membership cards, dues records, or signed statements by employees indicating their desire to be represented by the labor organization, or similar evidence acceptable to the Board, showing that at least 30 percent of the employees in the proposed unit wish to be represented by the petitioner.

(b) The contents of petitions filed under § 28.65(a)(2) shall conform to those provided for in paragraph (a) of this section, except that the information required by paragraphs (a)(4) and (a)(7) of this section need not be supplied. Additionally, a petition under § 28.65(a)(2) shall include evidence satisfactory to the Board that at least 30 percent of the employees in the unit no longer wish to be represented by the labor organization currently having bargaining rights.

(c) The contents of petitions filed under § 28.65(a)(3) shall conform to those provided in petitions under paragraph (a) of this section, except that the information required by paragraphs (a)(4) and (a)(7) of this section need not be supplied, but shall include a detailed statement giving the objective considerations which support the GAO's good faith reason for doubting the labor organization's continued status as the exclusive representative.

(d) The contents of petitions filed under § 28.65(a)(4) shall include the information required under paragraph (a) of this section, with the exception of the information required by paragraphs (a)(4) and (a)(7) of this section. Also, instead of the information required in paragraph (a)(1) of this section, the petition shall identify the existing unit and the date the organization was recognized by the GAO or certified as the exclusive representative, and shall explain the changes desired in the unit and the reasons therefor.

(e) Petitions under § 28.65(a)(5) shall be filed on forms to be supplied by the Board, upon request.

§ 28.69 Pre-investigation proceedings.

(a) Upon the filing of a valid petition, the General Counsel may request GAO to notify employees as to the existence of the petition by posting a notice for at least 10 days in locations appropriately selected to reach all employees in the unit covered by the petition. The notice shall include a request that the Board's General Counsel be notified of the existence of any other interested parties.

(b) GAO shall supply the General Counsel with any information in its possession concerning other potentially interested labor organizations, copies of relevant correspondence, and copies of existing or recently expired agreements covering any employees in the unit. The GAO shall also provide a list of employees it believes should be included in the unit together with their classifications and the names and classifications of those employees it proposes to exclude from the unit.

(c) All interested parties shall meet as soon as possible after the expiration of the ten-day posting period and shall attempt to resolve any issues in controversy.

(d) A labor organization may become an intervenor in any representation proceeding by satisfying the General Counsel within the ten-day posting period that it represents at least ten percent of the employees in the proposed unit or submits other evidence that it is the exclusive representative of the employees involved.

§ 28.71 Processing petitions.

(a) Upon the expiration of the ten-day posting period, and after the General Counsel considers an appropriate period has elapsed for consultation among the parties to resolve or identify issues, the General Counsel shall prepare a report to the Board which may recommend:

(1) Approval of any agreement entered into by the parties during their consultations including an agreement on the appropriate units, on the withdrawal of the petition, or on a joint request to conduct an election to determine which labor organization, if any, the employees select to be their exclusive bargaining representative;

(2) Dismissal of the petition as being without merit; or

(3) Issuance of a notice of hearing for the purpose of disposing of the remaining issues raised in the petition.

(b) The General Counsel's report shall be supplied to all interested parties, and, unless all parties agree to a shorter period, they shall have 15 days during which to file any response with the Board.

(c) The Board, as expeditiously as feasible after the expiration of the period specified in paragraph (b) of this section, but no later than 30 days thereafter, shall either approve the report and order appropriate steps to carry out its recommendations, or remand it to the General Counsel with further instructions.

(d) Where a hearing is ordered, a Hearing Officer shall be designated by the Board. The report of the Hearing Officer shall include Findings of Fact and Recommendations.

(e) After receiving the report from the Hearing Officer, and after providing the parties with an opportunity for comment, the Board shall issue a Decision and Order determining the appropriate unit, directing an election, dismissing the petition or making some other appropriate disposition of the matter.

(f) Final Decisions and Orders issued by the Board based on hearings held in accordance with paragraphs (d) and (e) of this section shall not be considered final decisions subject to appeal before the Circuit Courts of Appeal.

§ 28.73 Conduct of elections.

(a) The Board shall supervise any election it orders to be conducted, but may delegate ministerial functions relating to an election to any qualified independent organization; to members of the Board's full-time staff; or to temporary employees hired for this purpose.

(b) Appropriate notices setting forth details of the election shall be posted by GAO as directed by the Board.

(c) The Board shall, through its agents chosen to conduct the election:

(1) Provide the opportunity for all qualified voters to indicate their choices in secrecy;

(2) Offer qualified voters the opportunity to vote for any labor organization on the ballot, or to reject all labor organizations;

(3) Permit all parties to observe all aspects of the election procedure other than any which would interfere with the secrecy of the ballot;

(4) Provide for all parties to challenge the eligibility of any voters, and to impound the ballots of such voters, subject to later determination of eligibility should the number of challenges potentially affect the results;

(5) Certify to all parties the results of the election.

(d) Upon receiving a report of the results of the election, the Board shall:

(1) If necessary rule on the challenges and adjust the results accordingly;

(2) Formally announce the results and, where appropriate, designate a labor organization as the exclusive collective bargaining agent, or withdraw such a designation;

(3) Where one or more of the labor organizations on the ballot has received the vote of 30% of the employees eligible to vote, but none has gained a majority of the votes cast, order a runoff election between the two choices receiving the largest number of votes in the original election, unless, because of a tie vote or for some other reason, the result is inconclusive; and,

(4) Where the result is inconclusive, conduct no more than one additional election on that petition to clarify the result.

Subpart F—Special Procedures—Unfair Labor Practices

§ 28.81 Authority of the Board.

(a) The procedures in this subpart relate in part to the Board's functions "to consider and order corrective or disciplinary action in cases arising from *** a matter appealable to the Board under the labor-management relations program under" 31 U.S.C. 732(e)(2) "including a labor practice prohibited under 31 U.S.C. 732(e)(1). 753(a)(6).

(b) The system so established by the Comptroller General is required to provide that each employee of the GAO has the right to form, join or assist, or not form, join or assist an employee organization, freely and without penalty or reprisal and for a labor-management relations program, consistent with Chapter 71 of Title 5, U.S.C. (31 U.S.C. 732(3)).

[47 FR 56981, Dec. 22, 1982]

§ 28.83 Unfair labor practices—Board procedures.

(a) Unfair labor practices are defined at GAO Order 2711.1 dated October 1, 1980. An allegation that a provision of GAO Order 2711.1 is inconsistent with Chapter 71 of Title 5, United States Code, and thereby denies to an employee or labor organization rights comparable to those granted by Chapter 71 of Title 5, U.S. Code, may also be raised under the unfair labor practice procedure.

(b) An allegation that unfair labor practices have been committed shall be subject to the procedures appearing in Subpart B for the filing of petitions, response by the GAO, investigation by the General Counsel, and the Board's disposition, except as set forth in paragraph (c) of this section.

(c) No complaint will be issued based on any alleged unfair labor practice which occurred or was discovered more than 6 months before the filing of an unfair labor practice charge with the charged party, as provided in paragraph 14b of GAO Order 2711.1, or more than 9 months before the filing of a complaint/petition with the General Counsel.

§ 28.85 Negotiability issues—compelling need.

Where the GAO and an exclusive bargaining representative disagree on whether a matter is subject to negotiation as part of the requirement to bargain in good faith, the matter shall be appealable to the Board under the following procedures:

(a) When, in connection with negotiations, a proposal is declared nonnegotiable, the party submitting the proposal shall, prior to the close of negotiations, submit to the other party a

Request for Formal Negotiability Determination reciting the proposal in question. The party declaring the proposal nonnegotiable shall, within ten (10) days, deliver to the other party a Formal Negotiability Determination stating the basis for the Determination.

(b) A Formal Negotiability Determination may be appealed to the Board within 20 days from receipt by filing a Petition for Review with the Board. A complete statement of argument from the petitioner should accompany the Petition for Review.

(c) The Board shall serve the Respondent with a copy of the Petition for Review and accompanying argument. Respondent shall have 20 days in which to reply to the Petition for Review.

(d) One or more members of the Board shall review the arguments, hold a hearing if the Hearing Officer deems it necessary, and issue a decision.

(e) The decision shall become final in accordance with § 28.25.

§ 28.87 Standards of Conduct for Labor Organizations.

(a) The GAO shall only accord recognition to labor organizations that are free from corrupt influences and from influences opposed to basic democratic principles. An organization is not required to prove it is free from such influence if it is subject to governing requirements calling for the maintenance of:

(1) Democratic procedures;

(2) Freedom from totalitarian influence;

(3) Independence on the part of its agents and officers from any business or financial interests which represent conflicts of interest or potential conflicts of interest; and

(4) Fiscal integrity, including provision for the dissemination of regular financial reports to its members.

(b) A labor organization which has or seeks recognition as a representative of employees under this chapter shall file financial and other reports with the Board and comply with trusteeship and election standards.

(c) A labor organization which has or seeks recognition under these Rules, shall adhere to principles enunciated in the Regulations issued by the Assistant Secretary of Labor for Labor/Management Relations regarding standards of conduct for labor organizations in the public sector. Complaints of violations of this section shall be filed with the Board. In any matter arising under this section, the Board may require a labor organization to cease and desist from violations of this section and require it to take such actions as it considers appropriate to carry out the policies of this section.

(d) This chapter does not authorize participation in the management of a labor organization or acting as a representative of a labor organization by a management official, a supervisor, or a confidential employee, or by any employee if the participation or activity would result in a conflict or apparent conflict of interest or would otherwise be incompatible with law or with the official duties of the employee.

(e) In the case of any labor organization which by omission or commission has willfully and intentionally called or participated in a strike, work stoppage or slowdown, or picketed in a manner which interfered with the operations of a government agency, or has condoned such activity, the Board shall, upon an appropriate finding it has made of such a violation—

(1) Revoke the recognition status of the labor organization; or

(2) Take any other appropriate disciplinary action.

(f) The General Counsel may charge a labor organization with violations of this section. The Board shall conduct proceedings with regard to such charge and may require a labor organization to take such actions as it deems necessary to carry out the policies of this section.

§ 28.89 Review of arbitration awards.

(a) Either party to an arbitration proceeding conducted pursuant to a grievance procedure under a collective bargaining agreement may file an exception to the arbitrator's award within 30 days of its receipt, and shall serve such to all other parties.

(b) An opposition to the exception may be filed with the Board, and shall be served on all other parties, within 30 days after receipt of the exception.

(c) An exception shall be carefully documented as to the reasons therefor.

(d) The Board's decision regarding an exception shall be based on:

(1) A finding that the award is contrary to any law, rule, regulation, or Order; or

(2) Other grounds similar to those applied by federal courts in private sector labor-management relations.

(e) If no exception to an arbitrator's award is filed within 30 days after it is issued, the award shall be final and binding.

Subpart G—Disciplinary and Stay Proceedings

§ 28.101 General authority.

The procedures in this Subpart relate to the Board's functions "to consider, decide and order corrective or disciplinary action (as appropriate) in cases arising" from any area within the Board's jurisdiction.

§ 28.103 Investigative authority.

In addition to the authority vested by Subchapters III and IV of Chapter 7 of Title 31, U.S.C. in the General Counsel to investigate allegations of prohibited personnel practices and prohibited political activities, the Board may request the General Counsel to investigate any personnel matter in a case under the Board's jurisdiction to determine whether reasonable grounds exist upon which to initiate disciplinary action against an employee of GAO.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.105 Disciplinary proceedings.

(a) If the General Counsel determines after any investigation under § 28.103 or 31 U.S.C. 752(b) that disciplinary action should be initiated against an employee, the General Counsel shall prepare a written complaint against the employee containing his/her determination, together with a statement of the supporting facts, and present the complaint and the statement to the employee and the Board in accordance with paragraphs (b) and (c) of this section.

(b) In the case of an employee in a confidential, policy making, policy-determining, or policy-advocating position appointed by the President, by and with the advice and consent of the Senate, the complaint and statement referred to in paragraph (a) of this section, with any response by the employee, shall be presented to the Congress for appropriate action in lieu of being presented under paragraph (d) of this section.

(c) Any employee against whom a complaint has been presented to the Board under paragraph (a) of this section is entitled to:

(1) A reasonable time to answer orally and in writing and to furnish affidavits and other documentary evidence in support of the answer;

(2) Be represented by an attorney or other representative;

(3) A hearing before the Board or a member designated by the Board;

(4) Have a transcript kept of any hearing under paragraph (c)(3) of this section; and

(5) A written decision and reasons therefor at the earliest practicable date, including a copy of a final decision ordering disciplinary action.

(d) A final order of the Board may order disciplinary action consisting of removal, reduction in grade, debarment from GAO employment for a period not to exceed 5 years, suspension, reprimand, or an assessment of civil penalty not to exceed $1,000.

(e) There may be no administrative appeal from an order of the Board under paragraph (d) of this section. An employee subject to a final decision ordering disciplinary action under this section may obtain judicial review of the order in the United States Court of Appeals for the judicial circuit in which the employee resides or to the United States Court of Appeals for the District of Columbia in accordance with 31 U.S.C. 752.

[46 FR 35478, July 9, 1981, as amended at 47 FR 56981, Dec. 22, 1982]

§ 28.107 Stay proceedings.

(a) If the General Counsel determines after an investigation under these rules that there are reasonable grounds to believe that a personnel action was taken, or is to be taken, as a result of a prohibited personnel practice, the General Counsel may request any member of the Board to order a temporary stay of the personnel action for a period of not more than 60 days.

(b) A Board member shall order a temporary stay under paragraph (a) of this section unless the member determines that such a stay would not be appropriate. Unless denied, any temporary stay requested shall be granted within 3 working days after the date of request.

(c) The Board may grant a further temporary stay or a permanent stay if the Board concurs in the determination of the General Counsel and after an opportunity for oral or written comment by the General Counsel and GAO. A permanent stay by the Board is final and appealable in accordance with § 28.27.

Subpart H—Appeals by Members of the Senior Executive Service

§ 28.111 Personnel actions involving SES members.

Members of the GAO Senior Executive Service (SES) may appeal adverse actions relating to misconduct, malfeasance or similar action to the Board in accordance with Subpart B. Members of the GAO SES who allege that they have been subjected to a personnel action that constitutes a prohibited personnel practice or prohibited discrimination may appeal to the Board in accordance with Subpart B or Subpart D respectively.

§ 28.113 Performance based actions.

A career appointee removed from SES to a GAO position outside the SES for less than fully successful executive performance shall, upon notice of such removal, be entitled, upon request, to an informal hearing before a member of the Board designated by the Chairman of the Board. At the hearing the career appointee may appear and present arguments, but such hearing shall not give the career appointee the right to initiate an action with the Board under another provision of these rules, nor need the removal action be delayed as a result of the granting of such hearing.

Subpart I—Ex Parte Communications

SOURCE: 48 FR 29666, June 28, 1983, unless otherwise noted.

§ 28.117 Policy.

It is the policy of the Board to strictly regulate ex parte communications between members of the Board and their decision-making personnel and any interested party to a proceeding before the Board.

§ 28.119 Explanation and definitions.

(a) Ex parte communications are oral or written communications between decision-making personnel of the Board and an interested party to a proceeding without providing the other parties to the proceeding a chance to participate. Not all ex parte communications are prohibited, however, only those which involve the merits of the case or those which violate other rules requiring submissions to be in writing. Accordingly, interested parties may make inquiries about such matters as the status of a case, when it will be heard, and the method for transmitting evidence to the Board. Such communications should be directed to the Administrative Officer to the Board. Parties may not inquire about such matters as what defense they should use, whether their evidence is adequate, make a submission orally which is required to be in writing, or otherwise inquire as to the merits of a pending case.

(b) In this Subpart—

(1) "Interested party" includes:

(i) Any party, including the General Counsel of the Board, or representative of a party involved in a proceeding before the Board;

(ii) any person desiring to intervene in any proceeding before the Board; or

(iii) Any other person who might be affected by the outcome of a proceeding before the Board.

(2) "Decision-making personnel" means the Board, a panel of Board members, a Board member, a Hearing Officer and/or an employee of the Board, other than the General Counsel of the Board, who reasonably can be expected to participate in the decision-making process of the Board.

§ 28.121 Prohibited communications.

Ex parte communications concerning the merits of any matter before the Board for adjudication or which would otherwise violate rules requiring written submissions are prohibited from the time the interested party involved has knowledge that the matter may be considered by the Board until the Board has rendered a final decision on the case.

§ 28.123 Reporting of communications.

Any communication made in violation of this section shall be made a part of the record in the proceeding and an opportunity for rebuttal allowed. If the communication was oral, a memorandum stating the substance of the discussion shall be placed in the record.

§ 28.125 Sanctions.

The following sanctions shall be available for violations of this Subpart:

(a) The Board, a panel of Board members, a Board member or a Hearing Officer, as necessary, may, in the interest of justice, require the offending party to show cause why his/her claim, interest, motion or petition should not be dismissed, denied or otherwise adversely affected.

(b) The Board, a panel of Board members, a Board member or a Hearing Officer, as necessary, may invoke such sanctions against any offending party as may be appropriate under the circumstances.

SUBCHAPTER C—CLAIMS; GENERAL

PART 30—SCOPE OF SUBCHAPTER

AUTHORITY: 31 U.S.C. 711 and 3702.

§ 30.1 Coverage of regulations in Subchapter C.

The regulations in Subchapter C relate to all classes of claims by and against the United States except:

(a) Those claims which are under the exclusive jurisdiction of administrative agencies pursuant to specific statutory authority;

(b) Claims for charges for transportation services furnished for the account of the United States, which now are to be filed with the General Services Administration or the agencies out of whose activities they arise. However, claims by carriers and forwarders against the United States for amounts administratively deducted from transportation payment vouchers in connection with loss or damage to property are covered by this subchapter and are to be filed in the General Accounting Office.

[27 FR 12044, Dec. 6, 1962, as amended at 40 FR 60036, Dec. 31, 1975; 47 FR 56980, Dec. 22, 1982]

PART 31—CLAIMS AGAINST THE UNITED STATES; GENERAL PROCEDURE

Sec.
31.1 Scope of part.

FILING REQUIREMENTS FOR CLAIMANTS

31.2 Form of claim.
31.3 Claim filed by attorney or agent.
31.4 Where claims should be filed.
31.5 Statutory limitations on claims.

INFORMATION RELATING TO CLAIMS

31.6 Information relating to claims presented to the Claims Group, Accounting and Financial Management Division of the General Accounting Office.
31.7 Basis of claim settlements.
31.8 Form of claim settlements.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 31 U.S.C. 3702.

SOURCE: 22 FR 10890, Dec. 28, 1957, unless otherwise noted.

EDITORIAL NOTE: Nomenclature changes to Part 31 appear at 37 FR 26707, Dec. 15, 1972; 45 FR 22873, Apr. 4, 1980 and 45 FR 84955, Dec. 24, 1980.

§ 31.1 Scope of part.

This part prescribes general procedures applicable to claims against the United States which must be adjudicated in the General Accounting Office before payment is made or denied exclusive of transportation claims. Special procedures applicable to specified types or classes of claims against the United States are contained in the subsequent parts of this subchapter.

FILING REQUIREMENTS FOR CLAIMANTS

§ 31.2 Form of claim.

Unless otherwise specifically provided, claims will be considered only when presented in writing over the signature and address of the claimant or over the signature of the claimant's authorized agent or attorney. Generally, no particular form is required for filing a claim; however, claim forms are prescribed in succeeding parts of this subchapter for specific classes of claims.

§ 31.3 Claim filed by attorney or agent.

A claim filed by an agent or attorney must be supported by a duly executed power of attorney or other documentary evidence of the agent's or attorney's right to act for the claimant. See § 11.8 of this chapter.

[22 FR 10890, Dec. 28, 1957, as amended at 45 FR 84955, Dec. 24, 1980]

§ 31.4 Where claims should be filed.

Action will generally be expedited if claimants file their claims initially with the administrative department or agency out of whose activities they arose. Claims which cannot be disposed of administratively will be transmitted to the Claims Group, Accounting and Financial Management Division of the General Accounting Office by the administrative office. However, as to claim filing requirements when the statutory period of limitation is about to expire, see § 31.5. Claims filed direct with the General Accounting Office should be addressed to

Claims Group, Accounting and Financial Management Division,
U.S. General Accounting Office,
Washington, D.C. 20548.

[23 FR 7478, Sept. 26, 1958, as amended at 40 FR 60036, Dec. 31, 1975]

§ 31.5 Statutory limitations on claims.

(a) *Statutory limitations relating to claims generally.* Statutory limitations relating to claims generally are contained in 31 U.S.C. 3702(b). Claimants should submit their claims to the Claims Group, Accounting and Financial Management Division of the General Accounting Office if the statutory period of limitation will soon expire.

(b) *Statutory limitation on check claims.* The statutory limitation on claims on account of checks appearing to have been paid are contained in 31 U.S.C. 3702(c). To protect their own interests, it is the responsibility of claimants to present their claims for the proceeds of checks to the Treasurer of the United States or the General Accounting Office if the statutory period of limitation is about to expire.

(c) *Other statutory limitations.* It is not intended to imply that statutes of limitation imposed by Congress are necessarily limited to those cited in paragraphs (a) and (b) of this section. It is incumbent on claimants to inform themselves regarding other possible statutory limitations.

[23 FR 7478, Sept. 26, 1958, as amended at 40 FR 60036, Dec. 31, 1975; 47 FR 56980, Dec. 22, 1982]

INFORMATION RELATING TO CLAIMS

§ 31.6 Information relating to claims presented to the Claims Group, Accounting and Financial Management Division of the General Accounting Office.

Claimants or their authorized representatives may obtain information relating to claims which have been presented to the Claims Group, Accounting and Financial Management Division of the General Accounting Office by addressing correspondence to

Claims Group, Accounting and Financial Management Division,
U.S. General Accounting Office,
Washington, D.C. 20548.

or by calling in person at that Office at 441 G Street NW.

[23 FR 7478, Sept. 26, 1958, as amended at 40 FR 60036, Dec. 31, 1975]

§ 31.7 Basis of claim settlements.

Claims are settled on the basis of the facts as established by the Government agency concerned and by evidence submitted by the claimant. Settlements are founded on a determination of the legal liability of the United States under the factual situation involved as established by the written record. The burden is on claimants to establish the liability of the United States, and the claimants' right to payment. The settlement of claims is based upon the written record only.

§ 31.8 Form of claim settlements.

(a) *Allowed claims.* The Claims Group, Accounting and Financial Management Division of the General Accounting Office will certify claims for payment either by use of a Certificate of Settlement, GAO Form 39, or by certificate of allowance placed on the voucher when voucher procedures are in effect.

(b) *Disallowed claims.* When part of a claim is allowed and part disallowed, a statement relating to the disallowed portion will be included on the certificate of settlement or the voucher. When the full amount of a claim is disallowed, the claimant will be advised by issuance of Settlement Certificate, GAO Form 44.

[23 FR 7478, Sept. 26, 1958, as amended at 40 FR 60036, Dec. 31, 1975]

PART 32—REVIEW AND RECONSIDERATION OF GENERAL ACCOUNTING OFFICE CLAIMS SETTLEMENTS

Sec.
32.1 Who may obtain review.
32.2 Basis for request for review.
32.3 Return of check or warrant with request for review.

AUTHORITY: 31 U.S.C. 711.

SOURCE: 22 FR 10890, Dec. 28, 1957, unless otherwise noted.

§ 32.1 Who may obtain review.

Settlements made pursuant to 31 U.S.C. 3702 will be reviewed: (a) In the discretion of the Comptroller General upon the written application of: (1) A claimant whose claim has been settled or (2) the head of the department or Government established to which the claim or account relates, or (b) upon motion of the Comptroller General at any time.

[22 FR 10890, Dec. 28, 1957, as amended at 47 FR 56980, Dec. 22, 1982]

§ 32.2 Basis for request for review.

Applications for review of claim settlements should state the errors which the applicant believes have been made in the settlement and which form the basis of his request for reconsideration.

§ 32.3 Return of check or warrant with request for review.

Unless otherwise directed by the Comptroller General on the presentation of proper facts in the particular case, the check issued upon a settlement must not be cashed when its amount includes any item as to which review is applied for, but should accompany the application for review.

PART 33—DECEASED CIVILIAN OFFICERS AND EMPLOYEES; PROCEDURES FOR SETTLEMENT OF ACCOUNTS

Sec.
33.1 Scope of part.
33.2 Definitions.
33.3 Forms prescribed for procedures in this part.
33.4 Notifying employees: agency responsibility.
33.5 Designation of beneficiary.
33.6 Claims settlement jurisdiction.
33.7 Securing claim on employee's death.
33.8 Claims involving minors or incompetents.
33.9 Return of unnegotiated Government checks.
33.10 Applicability of general procedures.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 5 U.S.C. 5582 and 5583.

EDITORIAL NOTE: Nomenclature changes to Part 33 appear at 45 FR 22873, Apr. 4, 1980, and 45 FR 84955, Dec. 24, 1980.

§ 33.1 Scope of part.

(a) *Accounts covered by this part.* This part prescribes forms and procedures for the prompt settlement of accounts of deceased civilian officers and employees of the Federal Government and of the government of the District of Columbia (including wholly owned and mixed-ownership Government corporations), as contemplated by 5 U.S.C. 5581, 5582, 5583. The term "deceased employees" as used in this part includes former civilian officers and employees who die subsequent to separation from the employing agency.

(b) *Exceptions.* The procedures prescribed by this part do not apply to:

(1) Accounts of deceased officers and employees of the Federal land banks, Federal intermediate credit banks, or regional banks for cooperatives (see 5 U.S.C. 5581(1)).

(2) Payment of unpaid balance of salary or other sums due deceased Senators or officers or employees of the Senate (see 2 U.S.C. 36a; 5 U.S.C. 5581(1)).

(3) Payment of unpaid balance of salary or other sums due deceased Members of the House of Representatives (see 2 U.S.C. 38a). See § 33.6 for settlement of accounts of deceased officers and employees of the House of Representatives.

[33 FR 685, Jan. 19, 1968]

§ 33.2 Definitions.

The term "unpaid compensation," as defined in the act and when used in this part, means the pay, salary, or allowances, or other compensation due on account of the services of the decedent for the Federal Government or the government of the District of Columbia. It shall include, but not be limited to, (a) all per diem in lieu of subsistence, mileage, and amounts due in reimbursement of travel expenses, including incidental and miscellaneous expenses which are incurred in connection with the travel and for which reimbursement is due; (b) all allowances upon change of official station; (c) all quarters and cost-of-living allowances and overtime or premium pay; (d) amounts due for payment of cash awards for employees' suggestions; (e) amounts due as refund of salary deductions for United States Savings bonds; (f) payment for all accumulated and current accrued annual or vacation leave equal to the compensation the decedent would have received had he lived and remained in the service until the expiration of the period of such annual or vacation leave; (g) the amounts of all checks drawn in payment of such compensation which were not delivered by the Government to the officer or employee during his lifetime or of any unnegotiated checks returned to the Government because of the death of the officer or employee.

[26 FR 12275, Dec. 23, 1961]

§ 33.3 Forms prescribed for procedures in this part.

Forms prescribed for procedures in this part are:

Standard Forms

SF 1152 Designation of Beneficiary, Unpaid Compensation for Deceased Civilian Employee.

SF 1153 Claim of Designated Beneficiary and/or Surviving Spouse for Unpaid Compensation of Deceased Civilian Employee.

SF 1155 Claim for Unpaid Compensation of Deceased Civilian Employee (No Designated Beneficiary or Surviving Spouse).

[23 FR 7479, Sept. 26, 1958]

§ 33.4 Notifying employees; agency responsibility.

Each agency of the Government affected will bring to the attention of its civilian employees the provisions of the act relative to their right to designate a beneficiary or beneficiaries to receive the amounts due and the disposition to be made of unpaid amounts where no beneficiary or beneficiaries have been designated.

[22 FR 10891, Dec. 28, 1957]

§ 33.5 Designation of beneficiary.

(a) *Designation Form.* SF 1152, Designation of Beneficiary, Unpaid Compensation of Deceased Civilian Employee, is prescribed for use by employees in designating a beneficiary and in changing or revoking a previous designation. However, in the absence of the prescribed form, any designation, change, or cancellation of beneficiary witnessed and filed in accordance with the general requirements of this part shall be acceptable. Each agency subject to the provisions of the act will furnish the employee SF 1152 upon request therefor.

(b) *Who may be designated.* An employee may designate any person or persons as beneficiary. The term "person or persons" as used in this part includes a legal entity or the estate of the deceased employee.

(c) *Executing and filing a designation of beneficiary form.* The SF 1152 must be executed in duplicate by the employee and filed with the employing agency where the proper officer will sign it and insert the date of receipt in the space provided on each part, file the original, and return the duplicate to the employee. The designation will be filed in the particular office which authorizes payment of the employee's compensation, or such other place as the head of the agency may direct.

(d) *Effective period of a designation.* A designation of beneficiary, properly executed and filed in the agency of employment, unless earlier changed or revoked in writing, will be effective as long as employment by the same agency continues and thereafter until the employee is transferred or reemployed by the same or another department or agency of the Government. Should an employee resign and be reemployed, or be transferred to another agency, and desire the unpaid compensation to be paid to a designated beneficiary, another designation of beneficiary form must be executed, as directed in paragraph (c) of this section. If an amount should become due from the agency from which the employee was separated, it will be the responsibility of such agency to ascertain, prior to payment, if the employee was reemployed and executed a designation of beneficiary in connection with such employment, and to pay the compensation to any person or persons so designated. A new designation of beneficiary is not required as to an employee whose agency or site function, records, equipment, and personnel are absorbed by another agency.

(e) *Change or revocation of a designation.* A designation of beneficiary previously made may be changed or revoked as of a later date by the execution and filing of another SF 1152 by the employee, as directed in paragraph (c) of this section. When a designation of beneficiary is changed or revoked, the employing agency should return the earlier designation to the employee.

[22 FR 10891, Dec. 28, 1957, as amended at 28 FR 12923, Dec. 5, 1963]

§ 33.6 Claims settlement jurisdiction.

(a) District of Columbia, Canal Zone Government and Government corporations. Claims for unpaid compensation due deceased employees of the government of the District of Columbia and the Canal Zone Government on the Isthmus of Panama shall be paid by these entities and those of wholly owned and mixed ownership Government corporations may be paid by the corporations. 5 U.S.C. 5583(b).

(b) Other agencies. Except as otherwise provided in paragraph (c) of this section, claims for unpaid compensation due deceased employees of other agencies of the Federal Government, including officers and employees of the House of Representatives, may be paid by those agencies.

(c) General Accounting Office. Except as provided in paragraph (a) of this section, claims for unpaid compensation due deceased employees of the Federal Government will be paid only upon settlement by the Claims Group, Accounting and Financial Management Division of the General Accounting Office in the following cases:

(1) When doubt exists as to the amount or validity of the claim.

(2) When doubt exists as to the person(s) properly entitled to payment.

(3) When the claim involves uncurrent checks. Unnegotiated and/or undelivered checks for unpaid compensation due the decedent which are drawn on designated depositaries and have not been paid prior to the close of the fiscal year next following the fiscal year in which the checks were issued are uncurrent. Claims for the proceeds of such checks must be submitted to the Claims Group, Accounting and Financial Management Division of the General Accounting Office for settlement pursuant to the provisions of 31 U.S.C. 3328(b). The checks, if available, should accompany the claims.

(d) Payment as provided in paragraphs (a), (b), and (c) of this section shall be made to the person or persons surviving at date of death in the following order of precedence:

(1) To the beneficiary or beneficiaries designated by the employee in a writing received in the employing agency prior to his death;

(2) If there is no designated beneficiary, to the surviving spouse of the employee;

(3) If none of the above, to the child or children of the employee and decendents of deceased children by representation;

(4) If none of the above, to the parents of the deceased employee or the survivor of them;

(5) If none of the above, to the duly appointed legal representative of the estate of the deceased employee; and

(6) If none of the above, to the person or persons entitled under the laws of the domicile of the employee at the time of his death. 5 U.S.C. 5582(b).

When the person(s) otherwise entitled to payment has not submitted a claim and cannot be located within 3 years after the death of the employee, payment shall be made to the person(s) in the same class of entitlement, or in the absence of anyone in the same class then the person(s) next in order of precedence as described in this paragraph.

[37 FR 26291, Dec. 9, 1972, as amended at 40 FR 60036, Dec. 31, 1975; 47 FR 56980, Dec. 22, 1982]

§ 33.7 Securing claim on employee's death.

As soon as practicable after the death of a civilian employee included within the provisions of the act, the agency in which he or she was last employed, upon determining that unpaid compensation is due the decedent, will request each designated beneficiary or, if no beneficiary was designated, the surviving spouse, to execute SF 1153, Claim of Designated Beneficiary and/or Surviving Spouse for Unpaid Compensation of Deceased Civilian Employee. When there is no designated beneficiary or surviving spouse, the employing agency will furnish the person or persons next in order of precedence, in accordance with the first section of the act, 5 U.S.C. 61f, SF 1155, Claim for Unpaid Compensation of Deceased Civilian Employee (No Designated Beneficiary or Surviving Spouse). When the designated beneficiary is the estate of the decedent, the employing agency will furnish the legal representative, heir, or heirs of the decedent SF 1055, Claim Against the United States for Amounts Due in the Case of a Deceased Creditor, prescribed in Part 35 of this chapter, since this form will elicit the information required for settlement of such claims. Any assistance deemed necessary for the proper execution of the forms will be furnished to all claimants by the employing agency.

[22 FR 10891, Dec. 28, 1957]

§ 33.8 Claims involving minors or incompetents.

(a) If a guardian or committee has been appointed for a minor or incompetent appearing entitled to unpaid compensation, the claim should be supported by a short certificate of the court showing the appointment and qualification of the claimant in such capacity.

(b) If no guardian or committee has been or will be appointed, the initial claim should be supported by a statement showing: (1) Claimant's relationship to the minor or incompetent, if any; (2) the name and address of the person having care and custody of the minor or incompetent; (3) that any moneys received will be applied to the use and benefit of the minor or incompetent; and (4) that the appointment of a guardian or committee is not contemplated.

[26 FR 12275, Dec. 23, 1961]

§ 33.9 Return of unnegotiated Government checks.

All unnegotiated U.S. Government checks drawn to the order of a decedent representing unpaid compensation as defined in § 33.2, and in the possession of the claimant, should be returned to the employing agency concerned. Claimants should be instructed to return any other U.S. Government checks, drawn to the order of a decedent for purposes other than unpaid compensation, such as veterans benefits, social security benefits, or Federal tax refunds, to the agency from which received with request for further instructions from that agency.

[23 FR 7479, Sept. 26, 1958]

§ 33.10 Applicability of general procedures.

When not in conflict with this part, the provisions of Part 31 of this subchapter relating to procedures applicable to claims generally, are also applicable to the settlement of accounts of deceased civilian officers and employees.

[22 FR 10891, Dec. 28, 1957]

PART 34—DECEASED MEMBERS OF THE ARMED FORCES AND NATIONAL GUARD; PROCEDURES FOR SETTLEMENT OF ACCOUNTS

Sec.

34.1 Scope of part.
34.2 Forms for filing claims.
34.3 Jurisdiction.
34.4 Furnishing forms and assistance to claimants.
34.5 Claims involving minors or incompetents.
34.6 Claims for unnegotiated Government checks.
34.7 Applicability of general claim procedures.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 10 U.S.C. 2771; 32 U.S.C. 714; sec. 3, 70A Stat. 619, as amended, 33 U.S.C. 857a; and sec. 4, 70A Stat. 619, as amended, 42 U.S.C. 213a.

SOURCE: 26 FR 12275, Dec. 23, 1961, unless otherwise noted.

EDITORIAL NOTE: Nomenclature changes to Part 34 appear at 45 FR 22873, Apr. 4, 1980, and 45 FR 84955, Dec. 24, 1980.

§ 34.1 Scope of part.

(a) This part prescribes forms and procedures for the prompt settlement of the accounts of:

(1) Deceased members of the Armed Forces (including deceased commissioned officers of the Public Health Service and the National Oceanic and Atmospheric Administration) pursuant to 10 U.S.C. 2771.

(2) Deceased members of the National Guard pursuant to 32 U.S.C. 714.

(b) A designation of beneficiary under 10 U.S.C. 2771 or 32 U.S.C. 714, properly executed and filed in the place designated for such purpose in the regulations of the department concerned, will be effective thereafter until:

(1) Expressly changed or revoked in writing or (2) the serviceman transfers to a different branch of the military service or (3) returns to the same or a different branch after a break in service.

(c) The term "deceased members" as used in the part includes former members who die subsequent to discharge or separation from the service.

(d) The payment provisions of 10 U.S.C. 2771 and 32 U.S.C. 714 are effective only when the member's death occurs on or after January 1, 1956. Claims relating to the accounts of members dying before such date are for consideration by the Claims Group, Accounting and Financial Management Division of the General Accounting Office.

(e) The term "pay and allowances" when used in this part includes any amount due a decedent from the service of which he was a member, exclusive of amounts payable administratively pursuant to other specific authority.

[33 FR 685, Jan. 19, 1968, as amended at 37 FR 26291, Dec. 9, 1972; 37 FR 26707, Dec. 15, 1972; 40 FR 60036, Dec. 31, 1975]

§ 34.2 Forms for filing claims.

The following standard forms are prescribed for use in the settlement of accounts to which this part relates:

SF 1174—Claim of Designated Beneficiary for Unpaid Pay and Allowances of Deceased Member of the Armed Forces.

SF 1175—Claim for Unpaid Pay and Allowances of Deceased Member of the Armed Forces (No Designated Beneficiary).

§ 34.3 Jurisdiction.

(a) *Administrative agencies.* Except as otherwise provided in paragraph (b) of this section, pay and allowances due deceased members of the Armed Forces and deceased members of the National Guard shall be paid by the military service or department concerned.

(b) *General Accounting Office.* Payments shall be made only upon settlement by the Claims Group, Accounting and Financial Management Division of the General Accounting Office in the following cases:

(1) When doubt exists as to the amount or validity of the claim.

(2) When doubt exists as to the person(s) properly entitled to payment.

(3) When the claim involves uncurrent checks. Unnegotiated and/or undelivered checks for pay and allowances due the decedent which are drawn on designated depositaries and have not paid prior to the close of the fiscal year next following the fiscal year in which the checks were issued are uncurrent. Claims for the proceeds of such checks must be submitted to the Claims Group, Accounting and Financial Management Division of the General Accounting Office for settlement pursuant to the provisions of 31 U.S.C. 3328(b). The checks, if available, should accompany the claims.

(c) Payment as provided in paragraphs (a) and (b) of this section shall be made to the person or persons surviving at date of death in the following order of precedence:

(1) Beneficiary designated by the member in writing to receive an amount, if the designation is received, before the deceased member's death, at the place named in the regulations prescribed by the Secretary concerned.

(2) Surviving spouse.

(3) Children and their descendants, by representation.

(4) Father and mother in equal parts or, if either is dead, the survivor.

(5) Legal representative.

(6) Person entitled under the law of the domicile of the deceased member.

When the person(s) otherwise entitled to payment has not submitted a claim and cannot be located within 3 years after the death of the member, payment shall be made to the person(s) in the same class of entitlement, or in the absence of anyone in the same class then the person(s) next in order of precedence as described in this paragraph.

[37 FR 26291, Dec. 9, 1972, as amended at 40 FR 60036, Dec. 31, 1975; 47 FR 56980, Dec. 22, 1982]

§ 34.4 Furnishing forms and assistance to claimants.

As soon as practicable after death of a member, the department under which the member was serving at date of death will furnish the designated beneficiary or beneficiaries Standard Form 1174, Claim of Designated Beneficiary for Unpaid Pay and Allowances of Deceased Member of the Armed Forces, for use in filing claim for any unpaid pay or allowances that may be due the decedent. If there is no designated beneficiary, the department will furnish the person or persons next in order of precedence, in accordance with 10 U.S.C. 2771(a) or 32 U.S.C. 714(a), SF 1175, Claim for Unpaid Pay and Allowances of Deceased Member of the Armed Forces (No Designated Beneficiary). Any assistance deemed necessary for the proper execution of the forms will be furnished to all claimants by the departments concerned.

§ 34.5 Claims involving minors or incompetents.

(a) If a guardian or committee has been appointed for a minor or incompetent appearing entitled to unpaid amounts, the claims should be supported by a short certificate of the court showing the appointment and qualification of the claimant in such capacity.

(b) If no guardian or committee has been or will be appointed, the initial claim should be supported by a statement showing (1) claimant's relationship to the minor or incompetent, if any; (2) the name and address of the person having care and custody of the minor or incompetent; (3) that any moneys received will be applied to the use and benefit of the minor or incompetent; and (4) that the appointment of a guardian or committee is not contemplated.

§ 34.6 Claims for unnegotiated Government checks.

Unnegotiated U.S. Government checks drawn to the order of the decedent by the service of which he was a member should be returned to the department concerned for consideration in connection with the settlement of the member's account. Claimants should be advised that all other unnegotiated U.S. Government checks drawn to the order of the decedent should be returned to the agency from which received with request for further instructions from that agency.

§ 34.7 Applicability of general claim procedures.

When not in conflict with this part, the provisions of Part 31 of this title, relating to procedures applicable to claims generally, are also applicable to the settlement of accounts of deceased members.

[33 FR 685, Jan. 19, 1968]

PART 35—DECEASED PUBLIC CREDITORS GENERALLY, CLAIM SETTLEMENT PROCEDURES

Sec.

35.1 Scope of part.
35.2 Form prescribed for procedures in this part.
35.3 Claim filing requirements.
35.4 Return of unnegotiated Government checks.
35.5 Claims involving minors.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 31 U.S.C. 3702.

SOURCE: 25 FR 6234, July 2, 1960, unless otherwise noted.

§ 35.1 Scope of part.

This part relates to the settlement of claims for amounts alleged to be due the estates of deceased individual public creditors, except when such claims are within the jurisdiction of administrative agencies pursuant to specific authority. The claims coming within the scope of this part include, among others, claims for amounts due deceased contractors (whether under terminated or continuing contracts) and other deceased public creditors for supplies furnished and services rendered.

[26 FR 12276, Dec. 23, 1961]

§ 35.2 Form prescribed for procedures in this part.

The following standard form is prescribed for use in filing claims on behalf of deceased public creditors: SF 1055—Claim Against the United States for Amounts Due in the Case of a Deceased Creditor.

§ 35.3 Claim filing requirements.

(a) *Use of prescribed form.* Claims to which this chapter relates, including claims for the proceeds of U.S. Government checks, will be filed on SF 1055.

(b) *Assisting claimants in filing claims.* Such assistance as is deemed necessary may be given to claimants by the administrative agencies to insure proper execution and submission of the claim forms, SF 1055.

(c) *Where claims should be filed.* Claims for amounts due deceased public creditors will be filed initially in the administrative office out of whose activities they arise.

§ 35.4 Return of unnegotiated Government checks.

All unnegotiated U.S. Government Checks in possession of a claimant which are drawn to the order of a deceased public creditor should be returned to the agency from which received.

§ 35.5 Claims involving minors.

(a) If a guardian has been appointed for a minor appearing entitled to unpaid amounts the claim should be supported by a short certificate of the court showing the appointment and qualification of the claimant in such capacity.

(b) If no guardian has been or will be appointed, the initial claim should be supported by a statement showing: (1) Claimant's relationship to the minor, if any; (2) the name and address of the person having care and custody of the minor; (3) that any moneys received will be applied to the use and benefit of the minor; and (4) that the appointment of a guardian is not contemplated.

[26 FR 12276, Dec. 23, 1961]

PART 36—INCOMPETENT PUBLIC CREDITORS; PROCEDURES FOR SETTLEMENT OF ACCOUNTS

Sec.

36.1 Scope of part.
36.2 Where claims should be filed.
36.3 Claim filing requirements.
36.4 Disposition of unnegotiated and undelivered Government checks.
36.5 Applicability of general claim procedures.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 31 U.S.C. 3702.

SOURCE: 23 FR 7480, Sept. 26, 1958, unless otherwise noted.

§ 36.1 Scope of part.

This part prescribed the procedures applicable to the settlement of claims for amounts due incompetent public creditors of the United States, including claims for the proceeds of Government checks drawn on the Treasurer of the United States or other authorized Government depository to the order of such creditors, except those claims which are under the exclusive jurisdiction of administrative agencies pursuant to specific statutory authority.

§ 36.2 Where claims should be filed.

Claims for amounts due incompetent public creditors will be filed initially with the Government agency out of whose activities they arise.

[33 FR 685, Jan. 19, 1968]

§ 36.3 Claim filing requirements.

(a) *Form of claim.* No form is prescribed for use in making claim for sums due incompetent creditors of the United States. Such claims must be filed in writing over the signature and full address of the person claiming on behalf of the incompetent creditor and must set forth the connection of the incompetent creditor with the United States Government, giving the name of the department, bureau, establishment or agency involved.

(b) *Claim filed by guardian or committee*—(1) *Initial claim.* The initial claim filed by the guardian or committee of the estate of an incompetent must be accompanied by a short certificate of the court showing the appointment and qualification of the claimant as guardian or committee.

(2) *Claims for recurring payments.* Subsequent claims from guardians or committees for recurring payments need not be accompanied by an additional certificate of the court, but they must be supported by a statement that the appointment is still in full force and effect.

(c) *Claims filed by other than guardian or committee.* When the amount due the incompetent is small and no guardian or committee of the estate has been or will be appointed, payment may be made, in the discretion of the Comptroller General, to the person or persons having care or custody of the incompetent, or to close relatives who will hold the amount for the use and benefit of the incompetent. The claim must be supported by a statement showing: (1) That no guardian or committee has been or will be appointed; (2) the claimant's relationship to the incompetent, if any; (3) the name and address of the person having care and custody of the incompetent; and (4) that any amount paid to the claimant will be applied to the use and benefit of the incompetent.

§ 36.4 Disposition of unnegotiated and undelivered Government checks.

All unnegotiated U.S. Government checks in possession of the claimant, drawn to the order of the incompetent public creditor and involved in the claim, should be returned to the agency from which received.

§ 36.5 Applicability of general claim procedures.

The provisions of Part 31 of this subchapter relating to the procedures applicable to claims generally are applicable also to the settlement of accounts of incompetent public creditors to which this chapter relates.

SUBCHAPTER D—TRANSPORTATION

PART 51—DETERMINATIONS

Sec.
51.1 Scope of part.
51.2 Standard forms and procedures.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 31 U.S.C. 3511 and 3512.

§ 51.1 Scope of part.

This part contains basic determinations by the Comptroller General as to the extent he deems it necessary to continue or discontinue to exercise the authority to prescribe forms and uniform procedures provided in 31 U.S.C. 3511.

[40 FR 47511, Oct. 9, 1975, as amended at 47 FR 56989, Dec. 22, 1982]

§ 51.2 Standard forms and procedures.

In connection with the audit of payments for transportation services furnished for the account of the United States and the adjustment of claims pertaining thereto, the Administrator, General Services Administration, may prescribe standard forms and procedures without consultation with the General Accounting Office, except that the prescription thereof is subject to the uniform standards and procedures necessary to permit performance of the discretionary function vested by statute in the Comptroller General and other uniform fiscal requirements deemed necessary, as prescribed in 4 CFR Part 52.

[47 FR 50843, Nov. 10, 1982]

PART 52—UNIFORM STANDARDS AND PROCEDURES FOR TRANSPORTATION TRANSACTIONS

Sec.
52.1 Scope of part.
52.2 Use of American flag vessels and certificated air carriers.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 31 U.S.C. 3511, 3512, 3513, 3526 and 3529; sec. 901(a), 49 Stat. 2015, 46 U.S.C. 1241(a); sec. 5, 88 Stat. 2104, 49 U.S.C. 1517.

§ 52.1 Scope of part.

This part contains uniform standards and procedures relating to discretionary functions vested by statute in the Comptroller General and to matters requiring uniformity of fiscal practices relating to transportation transactions entered into for the account of the United States Government.

[40 FR 47512, Oct. 9, 1975]

§ 52.2 Use of American flag vessels and certificated air carriers.

(a) *Transportation of passengers.* Section 901 of the Merchant Marine Act of 1936, 46 U.S.C. 1241, requires the use of American flag vessels for travel on official business; and section 5 of the International Air Transportation Fair Competitive Practices Act of 1974, 49 U.S.C. 1517, requires the use of air carriers certificated under section 401 of the Federal Aviation Act of 1958 (American flag) for Government-financed passenger transportation (including but not limited to Government dependents, consultants, grantees, contractors and subcontractors), when such carriers are available. Compliance with section 901 and section 5 is required whether the transportation expenses are paid by the United States or reimbursed to the traveler.

(b) *Transportation of personal effects and freight.* Section 901 of the Merchant Marine Act of 1936, 46 U.S.C. 1241, requires the use of American flag vessels by officers and employees of the United States for the transportation of their personal effects, when such vessels are available, and section 5 of the International Air Transportation Fair Competitive Practices Act of 1974, 49 U.S.C. 1517, requires the use of air carriers certificated under section 401 of the Federal Aviation Act of 1958 (American flag) for any Government-financed movement of freight by air when such air carriers are available.

(c) *Disallowance of expenditures.* The Comptroller General will disallow any expenditures for commercial non-American-flag air or foreign-flag ocean passenger transportation, or for foreign-flag ocean transportation of personal effects or non-American-flag air transportation of freight, unless there is attached to the payment voucher a certificate or memorandum adequately explaining why American-flag service was unavailable signed by the traveler or other responsible official of the agency authorizing the travel or transportation who has knowledge of the facts concerning such usage.

(d) *Required documentation.* Each voucher for reimbursement of expenses for travel in whole or in part via a non-American-flag air or foreign flag ocean carrier, and each bill for payment of transportation services furnished in whole or in part by a non-American-flag air or foreign flag ocean carrier will be supported by the following documentation:

(1) *Required certificate.* The certificate or memorandum required under this part should be substantially as follows:

I certify that it (is) (was) necessary for ———————— (name of traveler or agency) to use ———————— (foreign-flag vessel(s)) ———————— or noncertificated[1] air carrier(s) ———————— flight identification No(s). or to transport (personal effects) (freight) between ———————— and ———————— en route from ———————— to ———————— on ———————— (date) for the following reasons:

————————————————

————————————————

————————————————

————

Date

————————————————

Signature of traveler or authorizing officer

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Title or position

————————

Organization

(2) *Documentation for passenger and freight transportation by American-flag direct air carriers.* All bills submitted by American-flag direct air carriers for payment for commercial foreign air passenger or freight transportation must contain either: (i) A certification by the carrier that no non-American-flag air carriers were used in the carriage of the passenger or freight or (ii) copies of documents required to be retained by the carrier under 14 CFR Part 249 that would indicate which portion of the through movement was performed by American-flag and non-American-flag air carriers, together with the certificate required in paragraph (d)(1) of this section covering such usage.

(3) *Documentation by indirect air carriers.* All bills submitted by indirect air carriers as defined in 14 CFR 296.1 and 297.1 for the payment of transportation charges for the movement of freight by air must be supported by a copy of the air waybill and manifest required to be executed by 14 CFR 296.70 and 297.51.

(e) *Responsibility of carrier to secure certificate.* The certificate or memorandum required under paragraph (d)(1) of this section must be obtained by the ocean or air carrier or freight forwarder and submitted as support in billing charges for transportation services.

(f) *Responsibility of accountable officers.* Certifying officers and military disbursing officers have the responsibility in the first instance of determining the accuracy and acceptability of the certification or memorandum and other documentation required in paragraph (d) of this section which must be attached to bills involving transportation by non-American-flag air carriers and foreign-flag vessels prior to the certification of such bills. When there is doubt as to the acceptability of the certification, accountable officers or the head of the agency involved may request an advance decision by addressing a submission to the Comptroller General of the United States, U.S. General Accounting Office, Washington, D.C. 20548.

(g) *Responsibility of General Services Administration.* In auditing vouchers for payment of transportation charges to carriers and forwarders, the General Services Administration will ascertain that payments involving the use of a non-American-flag vessel or air carrier are supported by the required certificate or memorandum and documentation required in paragraph (d) of this section justifying such use. When there is doubt as to the accuracy or acceptability of any justification, the matter will be referred to the Comptroller General for decision.

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[1] Section 401 of Federal Aviation Act of 1958 (49 U.S.C. 1501).

[40 FR 47512, Oct. 9, 1975, as amended at 47 FR 56980, Dec. 22, 1982]

PART 53—REVIEW OF GENERAL SERVICES ADMINISTRATION TRANSPORTATION SETTLEMENT ACTIONS

Sec.
53.1 Definitions.
53.2 Actions reviewable by Comptroller General.
53.3 Requests for review.
53.4 Copies to General Services Administration.

AUTHORITY: 31 U.S.C. 711. Interpret or apply sec. 322, 54 Stat. 955, as amended, 49 U.S.C. 66(b).

SOURCE: 40 FR 47513, Oct. 9, 1975, unless otherwise noted.

§ 53.1 Definitions.

(a) "Claim" means any bill or demand, including submission of voucher or supplemental bill, for payment of charges for transportation and related services by a carrier or forwarder entitled under 49 U.S.C. 66 to payment for such services prior to audit by the General Services Administration.

(b) "Settlement" means any action taken by the General Services Administration in connection with the audit of payments for transportation and related services furnished for the account of the United States that has a dispositive effect, including:

(1) Deduction action (or refund by carrier) in adjustment of asserted transportation overcharges;

(2) Disallowance of a claim, or supplemental bill, for charges for transportation and related services, either in whole or in part;

(3) Any other action that entails finality of administrative consideration.

§ 53.2 Actions reviewable by Comptroller General.

Actions taken by the General Services Administration on a claim by a carrier or freight forwarder entitled under 49 U.S.C. 66 to be paid for transportation services prior to audit that have dispositive effect and constitute a settlement action as defined in § 53.1 will be reviewed by the Comptroller General, provided request for review of such action is made within six months (not including time of war) from the date such action is taken or within the periods of limitation specified in 49 U.S.C. 66(a), whichever is later.

§ 53.3 Requests for review.

Requests for review of settlement actions by the General Services Administration should be addressed to the Comptroller General of the United States, U.S. General Accounting Office, Washington, D.C. 20548. Each request for review must identify the transaction as to which review is requested by the date the action was taken, the Government bill of lading or Government transportation request number, the carrier's bill number, Government voucher number and date of payment, General Services Administration claim number, or other identifying information, to enable speedy location of the pertinent records. Each request for review should state why the action taken is believed erroneous and specify any factual, technical, or legal basis relied on.

§ 53.4 Copies to General Services Administration.

Review of settlement actions will be expedited if a copy of the document requesting review by the Comptroller General is sent to the General Services Administration to facilitate assembly of the pertinent records.

PART 56—JOINT REGULATIONS FOR ADVANCE PAYMENT OF CHARGES FOR TRANSPORTATION SERVICES FURNISHED THE UNITED STATES

Sec.
56.1 Prescription of standards.
56.2 Payment prior to Government confirmation of satisfactory performance.
56.3 Bonding requirements.

AUTHORITY: Sec. 1(b), 86 Stat. 1163, 1164, as amended by sec. 201, 88 Stat. 1959 (49 U.S.C. 66(c)).

SOURCE: 41 FR 53769, Dec. 9, 1976, unless otherwise noted.

§ 56.1 Prescription of standards.

The regulations in this part are issued jointly by the Comptroller General of the United States and the Secretary of the Treasury under the provisions of 49 U.S.C. 66(c) which authorizes payment of charges for transportation services to carriers or forwarders in advance of the completion of services without regard to 31 U.S.C. 3324: *Provided,* The carrier or forwarder has issued the usual ticket, receipt, bill of lading or equivalent document covering the service involved. Regulations, prescribed by the head of an agency in implementation of this part will be reviewed by the General Accounting Office as a part of its audit of the agency's activities.

[41 FR 53769, Dec. 9, 1976, as amended at 48 FR 4647, Feb. 2, 1983]

§ 56.2 Payment prior to Government confirmation of satisfactory performance.

Where a carrier or forwarder has issued the usual ticket, receipt, bill of lading or equivalent document, and subject to limitations prescribed by the Administrator, General Services Administration, or his designee, administrative procedures may provide for payment of bills for charges for transportation services furnished for the account of the United States prior to Government confirmation of the satisfactory completion of such services except those bills presented by:

(a) An assignee bank or financial institution under the authority of 31 U.S.C. 3727 and 41 U.S.C. 15;

(b) Payees who are in bankruptcy proceedings or are subject to the control of a receiver, trustee, or other similar representative;

(c) Payees who consistently fail to refund overcharges without assertion of substantial defenses or other valid reasons when notified by the General Services Administration or any other interested Government agency;

(d) Payees who without good cause fail to make timely disposition or settlement of loss or damage or other claims asserted by agencies of the United States;

(e) Payees owing substantial sums of money to the United States concerning which no adequate arrangements for settlement have been made;

(f) Payees in such bad financial condition as to justify a determination that the Government's best interests require consideration of special payment rules for their account;

(g) Payees who do business with the United States infrequently and who previously have not been administratively approved for payment upon presentation of bills;

(h) Any other person or business organization determined administratively for valid reasons to be ineligible for payment unless after review of the facts and in the absence of objection by the United States General Accounting Office it is determined administratively that the best interests of the United States will not be jeopardized by such payment.

[41 FR 53769, Dec. 9, 1976, as amended at 48 FR 4647, Feb. 2, 1983]

§ 56.3 Bonding requirements.

Whenever the head of an agency of the United States or his designee determines in any particular case that a bond (or other form of guarantee or assurance) of an acceptable surety is essential for the account of any particular carrier or forwarder in order to protect the interests of the United States where payments are to be made prior to Government confirmation of the satisfactory completion of transportation services a bond may be required and held by the agency making such requirement. The bond shall be for such amount as in the discretion of the responsible Government officers is necessary for the protection of the Government's best interests but shall not exceed $10,000 unless the head of the agency or his designee certifies that a bond for a higher amount is justified in the circumstances.

SUBCHAPTER E—STANDARDIZED FISCAL PROCEDURES

PART 75—CERTIFICATES AND APPROVALS OF BASIC VOUCHERS AND INVOICES

AUTHORITY: 31 U.S.C. 711 and 3511.

§ 75.1 Contractors' and vendors' certificates.

(a) The General Accounting Office no longer requires that a certificate as to correctness and nonpayment be executed on the bills and invoices of contractors and vendors, with the exception that carriers, or other corporations, agencies, or persons furnishing transportation and accessorial services to the Government must continue to execute the certificates as provided in Chapter 101, Part 41 of Title 41, Code of Federal Regulations. Pending the eventual elimination of the contractors' and vendors' certificates from all other standard voucher forms, the certificates on such other forms need no longer be executed. However, the elimination of this requirement does not dispense with the necessity for the specific certification of facts required by certain contracts.

(b) The omission of the certificate from bills or invoices submitted for payment to Government agencies does not in any manner lessen the responsibility of contractors and vendors in complying with all statutory requirements applicable to transactions with the Government, nor will it be construed as mitigating their liability for asserting false, fictitious, or fraudulent claims against the United States, penalties for which are set forth in 18 U.S.C. 287.

[22 FR 10906, Dec. 28, 1957, as amended at 47 FR 50843, Nov. 10, 1982; 47 FR 56980, Dec. 22, 1982]

SUBCHAPTER F—RECORDS

PART 81—PUBLIC AVAILABILITY OF GENERAL ACCOUNTING OFFICE RECORDS

Sec.

81.1 Purpose and scope of part.
81.2 Administration.
81.3 Definitions.
81.4 Requests for identifiable records.
81.5 Records originating outside GAO, or records involving work in progress.
81.6 Records which may be exempt from disclosure.
81.7 Fees and charges.
81.8 Public reading facility.

AUTHORITY: 31 U.S.C. 711.

SOURCE: 49 FR 38527, Oct. 1, 1984, unless otherwise noted.

§ 81.1 Purpose and scope of part.

This part implements the policy of the United States General Accounting Office (GAO) with respect to the public availability of GAO records. While GAO is not subject to the Freedom of Information Act (5 U.S.C. 552), GAO's disclosure policy follows the spirit of the act consistent with its duties and functions and responsibility to the Congress. Application of this act to GAO is not to be inferred from the provisions of these regulations.

§ 81.2 Administration.

The administration of this part is the duty and responsibility of the Director, Office of Policy (OP), United States General Accounting Office, 441 G Street, NW., Washington, D.C. 20548, and to that end the Director shall promulgate such supplemental rules or regulations as may be necessary.

§ 81.3 Definitions.

As used in this part:

(a) *"Identifiable"* means a reasonably specific description of a particular record sought, such as the date of the record, subject matter, agency or person involved, etc., which will permit location or retrieval of the record.

(b) *"Records"* includes all books, papers, manuals, maps, photographs, reports, and other documentary materials, regardless of physical form or characteristics under the control of GAO in pursuance of law or in connection with the transaction of public business. In the context of a request for a record or records, the term "records" refers only to a record in being and under the control of GAO. It does not include the compiling or procuring of a record. Nor does it include library or museum material made or acquired and preserved solely for reference or exhibition purposes, or extra copies of documents preserved only for convenience of reference. It is intended that GAO publications are not within the purview of this order. GAO published reports and decisions or listing of reports should be obtained from the U.S. General Accounting Office, Information Handling and Support Facility (IHSF), P.O. Box 6015, Gaithersburg, Md. 20877, phone (202) 275-6241.

(c) *"Records Available to the Public"* means records which may be examined or copied or of which copies may be obtained, in accordance with this part, by the public or representatives of the press regardless of interest and without specific justification.

(d) *"Disclose or Disclosure"* means making available for examination or copying, or furnishing a copy.

(e) *"Person"* includes an individual, partnership, corporation, association, or public or private organization other than a Federal agency.

§ 81.4 Requests for identifiable records.

(a) A request to inspect or obtain a copy of an identifiable record of GAO must be submitted in writing to the Director, OP (see § 81.2), who will promptly acknowledge and record the request.

(b) The Director, OP, or other GAO organizational unit will promptly honor the request if no valid objection exists to the propriety of such action and the requester is willing and able to pay the prescribed fees for making the record available for inspection or copying or being provided with a copy.

(c) In the event of an objection or doubt as to the propriety of providing the requester with a copy of the record sought, every effort will be made to resolve such problems as quickly as possible, including consultation with appropriate GAO elements. If it is determined that the record should be withheld, the Director, OP, shall inform the requester in writing that the request has been denied; shall identify the material withheld; and shall explain the basis for the denial.

(d) A person whose request is denied shall be informed that further consideration of his/her request may be obtained by a letter to the Comptroller General of the United States setting forth the basis for the belief that the denial of the request was unwarranted.

§ 81.5 Records originating outside GAO, or records involving work in progress.

(a) It is the policy of GAO not to provide records from its files that originate in another agency or nonfederal organization to persons who may not be entitled to obtain the records from the originator. In such instances, requesters will be referred to the person or organization that originated the records.

(b) In order to avoid disruption of work in progress, and in the interests of fairness to those who might be adversely affected by the release of information which has not been fully reviewed to assure its accuracy and completeness, it is the policy of GAO not to provide records which are part of ongoing reviews or other current projects. In response to such requests, GAO will inform the requester of the estimated completion date of the review or project so that the requester may then ask for the records. At that time, the records may be released unless exempt from disclosure under § 81.6.

§ 81.6 Records which may be exempt from disclosure.

The public disclosure of GAO records contemplated by this part does not apply to records, or parts thereof, within any of the categories listed below. Unless precluded by law, the Director, OP, may nevertheless release records within these categories.

(a) Congressional correspondence and other papers relating to work performed in response to a congressional request (unless authorized by the congressional requester), and congressional contact memoranda.

(b) Records specifically required by an Executive Order to be kept secret in the interest of national defense or foreign policy. An example of this category is a record classified under Executive Order 12356, National Security Information.

(c) Records related solely to the internal personnel rules and practices of an agency. This category includes, in addition to internal matters of personnel administration, internal rules and practices which cannot be disclosed without prejudice to the effective performance of any agency function. Examples within the purview of this exemption are guidelines, and procedures for auditors, investigators, or examiners.

(d) Records specifically exempted from disclosure by statute provided that such statute (1) requires that the matters be withheld from the public in such a manner as to leave no discretion on the issue, or (2) establishes particular criteria for withholding or refers to particular types of matters to be withheld.

(e) Records containing trade secrets and commercial or financial information obtained from a person and privileged or confidential. This exemption may include, but is not limited to, business sales statistics, inventories, customer lists, scientific or manufacturing processes or development information.

(f) Personnel and medical files and similar files the disclosure of which could constitute a clearly unwarranted invasion of personal privacy. This exemption excludes from disclosure all personnel and medical files, and all private or personal information contained in other files, which, if disclosed to the public, would amount to a clearly unwarranted invasion of the privacy of any person. An example of such other files within the exemption would be files compiled to evaluate candidates for security clearance.

(g) Investigatory files complied for law enforcement purposes.

(h) Records having information contained in or related to examination, operation, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions.

(i) Records containing geological and geophysical information and data (including maps) concerning wells.

(j) Inter-agency or intra-agency memoranda, letters or other materials that are part of the deliverative process. For example, this exemption includes internal communications such as GAO or other agency draft reports, and those portions of internal drafts, memoranda and workpapers containing opinions, recommendations, advice or evaluative remarks of GAO employees. This exemption seeks to avoid the inhibiting of internal communications, and the premature disclosure of documents which would be detrimental to an agency function.

(k) Records in addition to those described in paragraph (j) of this section containing information customarily subject to protection as privileged in a court or other proceedings, such as information protected by the doctor-patient, attorney-work product, or lawyer-client privilege.

(l) Unsolicited records containing information submitted by any person to GAO in confidence and records which GAO has obligated itself not to disclose. An example of records covered by this exemption would be information obtained by the GAO Fraud Referral and Investigations Group (GAO Hotline).

§ 81.7 Fees and charges.

(a) No fee or charge will be made for:

(1) Records provided under provisions of this part when the direct search and reproduction costs are less than $25.

(2) Records requested which are not found or which are determined to be exempt under provisions of this part.

(3) Staff-hours spent in resolving any legal or policy questions pertaining to the request.

(4) Copies of records including those certified as true copies, that are furnished for official use to any officer or employee of the federal government.

(5) When necessary or desirable to the performance of a function of GAO, copies of pertinent records furnished to a party having a direct and immediate interest in a matter pending before the Office.

(b) When costs are $25 or more, the fees and charges described below, will be assessed for the direct costs of search and reproduction of records available to the public under this part.

(1) The reproduction charge per page shall be 20 cents.

(2) Certification of authenticity shall be $10 for each certificate.

(3) Search for records by Office personnel:

(i) Clerical personnel—$7 an hour.

(ii) Professional personnel—$18 an hour.

(4) Other direct costs related to the request may be charged for such items as computer searches.

(c) GAO shall notify the requester and may require an advance deposit where the anticipated fees will exceed $50.

(d) Fees and charges shall be paid by check or money order payable to the U.S. General Accounting Office.

(e) Fees established by this section may be waived or reduced upon a determination by the Director, OP, that such waiver or reduction is in the public interest because furnishing the information is considered as primarily benefiting the general public. Persons seeking such waiver or reduction of fees may be required to submit a statement setting forth the intended purpose for which the records are requested or otherwise indicate how disclosure will primarily benefit the public and, in appropriate cases, explain why the volume of records requested is necessary. Determinations pursuant to this subsection are solely within the discretion of GAO.

§ 81.8 Public reading facility.

A public reading facility shall be maintained by the General Accounting Office at 441 G Street, NW., Washington, D.C. The facility, under the immediate supervision of the Chief, Legal Information and Reference Services, Office of the General Counsel, shall be open to the public from 8 a.m. to 5 p.m. except Saturdays, Sundays, and holidays.

PART 82—FURNISHING RECORDS OF THE GENERAL ACCOUNTING OFFICE IN JUDICIAL PROCEEDINGS

Sec.
82.1 Court subpoenas or requests.
82.2 Fees and charges.

AUTHORITY: 31 U.S.C. 711, 713, 714, 718, 3523, 2524, 2526, and 3529.

§ 82.1 Court subpoenas or requests.

(a) A subpoena or request from a court for records of the General Accounting Office should be directed to the Comptroller General of the United States and served upon the Records Management and Services Officer, Office of Information Systems and Services.

(b) In honoring a court subpoena or request original records may be presented for examination but must not be presented as evidence or otherwise used in any manner by reason of which they may lose their identity as official records of the General Accounting Office. They must not be marked or altered, or their value as evidence impaired, destroyed, or otherwise affected. In lieu of the original records, certified copies will be presented for evidentiary purposes since they are admitted in evidence equally with the originals (31 U.S.C. 704).

[33 FR 358, Jan. 10, 1968, as amended at 45 FR 84955, Dec. 24, 1980; 47 FR 56980, Dec. 22, 1982]

§ 82.2 Fees and charges.

The provisions of § 81.7 of this chapter are applicable to this part; however, where the charging of fees is appropriate, they need not be collected in advance.

[33 FR 358, Jan. 10, 1968, as amended at 47 FR 56980, Dec. 22, 1982]

PART 83—PRIVACY PROCEDURES FOR PERSONNEL RECORDS

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APPENDIX I—MEMORANDUM OF UNDERSTANDING

AUTHORITY: 31 U.S.C. 711(1); Memorandum of Understanding between the U.S. Office of Personnel Management, the National Archives and Records Service of the General Services Administration and the U.S. General Accounting Office; 4 CFR Part 81; 5 CFR Parts 294-297; and 31 U.S.C. 731, *et seq.*

SOURCE: 50 FR 13162, Apr. 3, 1985, unless otherwise noted.

§ 83.1 Purpose and scope of part.

This part describes the policy and prescribes the procedures of the United States General Accounting Office (GAO) with respect to maintaining and protecting the privacy of GAO personnel records. While GAO is not subject to the Privacy Act (Act) (5 U.S.C. 552a), GAO's policy is to conduct its activities in a manner that is consistent with the spirit of the Act and its duties, functions, and responsibilities to the Congress. Application of the Privacy Act to GAO is not to be inferred from the provisions of these regulations. These regulations are designed to safeguard individuals against invasions of personal privacy by requiring GAO, except as otherwise provided by law, to—

(a) Protect privacy interests of individuals by imposing requirements of accuracy, relevance, and confidentiality for the maintenance and disclosure of personnel records;

(b) Inform individuals of the existence of systems of personnel records maintained by GAO containing personal information: and

(c) Inform individuals of the right to see and challenge the contents of personnel records containing information about them.

This part applies to all systems of personnel records (as defined in § 83.3(g)) for which GAO is responsible.

§ 83.2 Administration.

The administration of this part is the duty and responsibility of the Director, Personnel, United States General Accounting Office, 441 G Street NW., Washington, D.C. 20548. To this end, the Director, Personnel, in consultation with the Office of the General Counsel, is authorized to issue such supplemental regulations or procedural directives as may be necessary and appropriate.

(a) The Director, Personnel, shall have general responsibility and authority for implementing this part, including—

(1) Approving all systems of personnel records to be maintained by GAO (whether physically located in GAO's Office of Personnel or elsewhere), including the contents and uses of such systems, accounting methods, and security methods; and

(2) Responding to an individual's request to gain access to or amend his or her own personnel records.

(b) The Director, Personnel, may delegate within GAO any of his functions under this part.

§ 83.3 Definitions.

As used in this part:

(a) "Individual" means a citizen of the United States or an alien lawfully admitted for permanent residence;

(b) "Information" means papers, records, photographs, magnetic storage media, micro storage media, and other documentary materials, regardless of physical form or characteristics, containing data about an individual and required by GAO in pursuance of law or in connection with the discharge of official business, as defined by statute, regulation, or administrative procedure;

(c) "Maintain" includes to collect, to use, or to disseminate;

(d) "Personnel record" means any record concerning an individual which is maintained pursuant to GAO's personnel management process or personnel policy setting process;

(e) "Record" means any item, collection, or grouping of information about an individual that is maintained by GAO, including, but not limited to, education, financial transactions, medical history, criminal history, or employment history, that contains the name or other identifying particular assigned to the individual, such as a fingerprint, voice print, or a photograph;

(f) "Routine use" means the disclosure of a record for a purpose which is compatible with the purpose for which it was collected;

(g) "System of personnel records" means a group of personnel records under the control of GAO from which information is retrieved by the name of the individual or by some identifying number, symbol, or other indentifying particular assigned to the individual; and,

(h) "System manager" means the Director of Personnel, his designee, or other GAO official designated by the Comptroller General, who has the authority to decide matters relative to systems of personnel records maintained by GAO.

§ 83.4 Conditions of disclosure.

GAO shall not disclose any record that is contained in a system of personnel records by an means of communication to any person or organization, including another agency, without the prior written consent of the individual to whom the record pertains, unless disclosure of the record would be:

(a) To those officers and employees of GAO who have a need for the record in the performance of their duties; or

(b) Required under regulations implementing the public availability of GAO records published at Part 81 of this chapter, or authorized under § 83.5; or

(c) For a routine use as defined in § 83.3(f); or

(d) To a recipient who has provided GAO with advance adequate written

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assurance that the record will be used solely as a statistical research or reporting record, and the record is to be transferred in a form that is not individually identifiable; or

(e) To another agency or an instrumentality of any governmental jurisdiction within or under the control of the United States for a civil or criminal law enforcement activity if the activity is authorized by law, if the head of the agency or instrumentality has made a written request to GAO specifying the particular record desired and the law enforcement activity for which the record is sought; or

(f) To any person pursuant to a showing of compelling circumstances affecting the health or safety of an individual (not necessarily the data subject) if upon such disclosure notification is transmitted to the last known address of the subject of the personnel record; or

(g) To either House of Congress, or, to the extent of matter within its jurisdiction, any committee or subcommittee of Congress; or

(h) Pursuant to the order of a court of competent jurisdiction or in connection with any judicial or quasi-judicial proceedings; or

(i) To the Bureau of the Census for purposes of planning or carrying out a census or survey or related activity pursuant to the provisions of Title 13, United States Code; or

(j) To the National Archives of the United States as a record which has sufficient historical or other value to warrant its continued preservation by the United States Government, or for evaluation by the Administrator of General Services or his designee to determine whether the record has such value; or

(k) To a consumer reporting agency in accordance with 31 U.S.C. 3711(f).

§ 83.5 Specific disclosure of information.

(a) This section governs responses to a member of the public, prospective employers, and law enforcement officials, for access to information covered by this part. It does not limit in any way other disclosures of information pursuant to other provisions of this part.

(b) The following information about most present and former GAO employees is available to the public:

(1) Name;

(2) Present and past position titles;

(3) Present and past grades;

(4) Present and past salaries; and

(5) Present and past duty stations (which include room numbers, shop designations, or other identifying information regarding buildings or places of employment.

(c) Disclosure of the above information will not be made where the information requested is a list of present or past position titles, grades, salaries, and/or duty stations of Government employees which, as determined by the Director, Personnel, is:

(1) Selected in such a way as to constitute a clearly unwarranted invasion of personal privacy because the nature of the request calls for a response that would reveal more about the employees on whom information is sought than the five enumerated items; or

(2) Would otherwise be protected from mandatory disclosure under an exemption of Part 81 of this title concerning the public availability of GAO records.

(d) In addition to the information that may be made available under paragraph (a) of this section, GAO may make available the following information to a prospective employer of a GAO employee or former GAO employee:

(1) Tenure of employment;

(2) Civil service status;

(3) Length of service in GAO and the Government; and

(4) When separated, the date and reason for separation shown on the required standard form.

(e) In addition to the information to be made available under paragraph (a) of this section, the home address of an employee shall be made available to a police or court official on receipt of a proper request stating that an indictment has been returned against the employee or that complaint, information, accusation, or other writ involving nonsupport or a criminal offense has been filed against the employee and the employee's address is needed for service of a summons, warrant, subpoena, or other legal process.

(f) Except as provided in paragraphs (a) through (e) of this section, and except as provided in this part, information required to be included in an Official Personnel Folder is not available to the public and is protected from disclosure by § 81.6(f) of this chapter.

(g) *Personnel Appeal Files.* (Those records maintained by the General Accounting Office Personnel Appeals Board of petitions or appeals filed with the Board by GAO employees, former employees, or applicants for employment. Such records do not include any of the investigative files or reports of the Personnel Appeals Board General Counsel. See 4 CFR 28.18(c)). GAO, upon receipt of a request which identifies the individual from whose file the information is sought, shall disclose the following information from a Personnel Appeal File to a member of the public, except when the disclosure would constitute a clearly unwarranted invasion of personal privacy:

(1) Confirmation of the name of the individual from whose file the information is sought and the names of the other parties concerned;

(2) The status of the case;

(3) The decision on the case;

(4) The nature of the action appealed; and

(5) With the consent of the parties concerned, other reasonably identified information from the file.

(h) *Leave Records.* The annual and sick leave record of an employee, or information from these records, is not to be made available to the public by GAO or other Government agency.

(i) *Examinations and Related Subjects.* Information concerning the results of examinations will be released only to the individual concerned, and to those parties explicitly designated in writing by the individual. The names of applicants for GAO positions or eligibles on GAO or civil service registers, certificates, employment lists, or other lists of eligibles, or their ratings or relative standings are not information available to the public.

(j) *Investigations.* (1) Upon written request, GAO will disclose to the parties concerned any report of personnel investigation under its control, or an extract of the report, to the extent the report is involved in a processed before GAO. For the purpose of this paragraph, the "parties concerned" means the Government employee involved in the proceeding, his or her representative designated in writing, and the representative of GAO involved in the proceeding. Where GAO obtains reports of personnel investigations or information from such reports from other government agencies on condition that it not release such data, GAO will refer parties requesting such information to the originating agency where their request will be processed.

(2) GAO will not make a report of investigation or information from a report under its control available to the public or to witnesses, except as otherwise required under GAO regulations implementing the public availability of records published at Part 81 of this chapter.

§ 83.6 Accounting of certain disclosures.

(a) With respect to each system of personnel records, GAO shall, except for disclosures made under §§ 83.4(a) and 83.4(b), keep an accurate accounting of—

(1) The date, nature, and purpose of disclosure of a record to any person; and

(2) The name and address of the person, agency, or organization to whom the disclosure is made.

(b) Such accounting shall be retained for at least 3 years or the life of the record, whichever is longer, after the disclosure for which the accounting is made.

(c) Except for disclosures made under § 83.4(e), the accounting shall be available upon written request to the individual named in the record.

§ 83.7 GAO policy and requirements.

(a) GAO shall maintain in its personnel records only such information about an individual as is relevant and necessary to accomplish an authorized official purpose. Authority to maintain personnel records does not constitute authority to maintain information in the record merely because a need for it may develop in the future. Both Government-wide and internal agency personnel records shall contain only information concerning an individual that is relevant and necessary to accomplish GAO's personnel management objectives as required by statute, GAO internal directive, or formal agreements between GAO and other Federal agencies.

(b) GAO shall make every reasonable effort to collect information about an individual directly from that individual when the information may result in adverse determinations about the individual's rights, benefits, and privileges under Federal programs. Factors to be considered in determining whether to collect the data from the individual concerned or a third party are:

(1) The nature of the information is such that it can only be obtained from another party;

(2) The cost of collecting the information directly from the individual is unreasonable when compared with the cost of collecting it from another party;

(3) There is virtually no risk that information collected from other parties, if inaccurate, could result in a determination adverse to the individual concerned;

(4) The information supplied by an individual must be verified by another party; or

(5) Provisions are made, to the greatest extent practical, to verify information collected from another party with the individual concerned.

(c) GAO shall inform each individual whom it asks to supply information for a personnel record, on the form which it uses to collect the information or on a separate form that can be retained by the individual, of—

(1) The authority for the solicitation of the information and whether disclosure of such information is mandatory or voluntary;

(2) The principal purpose or purposes for which the information is intended to be used;

(3) The routine uses which may be made of the information, as published pursuant to paragraph (d)(4) of this section; and

(4) The effects, if any, of not providing all or any part of the requested information;

(d) Subject to the provisions of paragraph (i) of this section, GAO shall publish in the FEDERAL REGISTER, upon establishment or revision, a notice of the existence and character of its systems of personnel records. Such notice shall include—

(1) The name and location(s) of each system of personnel records;

(2) The categories of individuals about whom records are maintained in each such system;

(3) The categories of records maintained in each system of personnel records;

(4) Each routine use of the records contained in each system of personnel records, including the categories of users and the purpose(s) of such use;

(5) The policies and practices of GAO regarding storage, retrievability, access controls, retention, and disposal of the records;

(6) The title and business address of the GAO official who is responsible for maintaining each system of personnel records;

(7) GAO procedures whereby an individual can ascertain whether a system of personnel records contains a record pertaining to the individual;

(8) Procedures whereby an individual can request access to any record pertaining to him contained in any system of personnel records, and how the individual may contest its content; and

(9) The categories of sources of records in each system of personnel records.

(e) GAO shall maintain all records which it uses in making any determination about any individual with such accuracy, relevancy, timeliness, and completeness as is reasonably necessary to assure fairness to the individual in the determination;

(f) GAO shall, prior to disseminating any record about an individual to any person other than a Federal agency, make all reasonable efforts to reassure that such records are accurate, complete, timely, and relevant for GAO's purposes;

(g) GAO shall make reasonable efforts to serve notice on an individual or his authorized representative when any personnel record on such individual is being made available to any person under compulsory legal process as soon as practicable after service of the subpoena or other legal process;

(h) GAO shall establish rules of conduct for persons involved in the design, development, operation, or maintenance of any system of personnel records or files or in maintaining any record, and to instruct each person with respect to such rules and requirements of this part, including any other rules and procedures adopted pursuant to this part;

(i)(1) GAO shall establish and maintain appropriate administrative, technical and physical safeguards to ensure the security and confidentiality of personnel records. At a minimum, these controls shall require that all persons whose official duties require access to and use of personnel records be responsible and accountable for safeguarding those records and for ensuring that the records are secured whenever they are not in use or under the direct control of authorized persons. Generally, personnel records should be held, processed, or stored only where facilities and conditions are adequate to prevent unauthorized access;

(2) Except for access by the data subject, only employees whose official duties require and authorize access shall be allowed to handle and use personnel records, in whatever form or media the records might appear. To the extent feasible, entry into personnel record storage areas shall be similarly limited. Documentation of the removal of records from storage areas must be kept so that adequate control procedures can be established to assure that removed records are returned intact on a timely basis and properly controlled during such period of removal.

(3) In addition to following the above security requirements, managers of automated personnel records shall establish and maintain administrative, technical, physical, and security safeguards for data about individuals in automated records, including input and output documents, reports, punched cards, magnetic tapes, disks, and on-line computer storage. As a minimum, the safeguards must be sufficient to:

(i) Prevent careless, accidental, or unintentional disclosure, modification, or destruction of identifiable personal data;

(ii) Minimize the risk of improper access, modification, or destruction of identifiable personnel data;

(iii) Prevent casual entry by persons who have no official reason for access to such data;

(iv) Minimize the risk of unauthorized disclosure where use is made of identifiable personal data in testing of computer programs;

(v) Control the flow of data into, through, and from computer operations;

(vi) Adequately protect identifiable data from environmental hazards and unnecessary exposure; and

(vii) Assure adequate internal audit procedures to comply with these procedures.

(4) The disposal of identifiable personal data in automated files is to be accomplished in such a manner as to make the data unobtainable to unauthorized personnel. Unneeded personal data stored on reusable media, such as magnetic tapes and disks, must be erased prior to release of the media for reuse.

(j) At least 30 days prior to publication of information under paragraph (d)(4) of this section, GAO shall publish in the FEDERAL REGISTER notice of any new use or intended use of the information in the system, and provide an opportunity for interested persons to submit written data, views, or arguments to GAO.

§ 83.8 Standards of conduct.

(a) GAO employees whose official duties involve the maintenance and handling of personnel records shall not disclose information from any personnel record unless disclosure is part of their official duties or required by statute, regulation, or internal procedure.

(b) Any GAO employee who makes an unauthorized disclosure of personnel records or a disclosure of information derived from such records, knowing that such disclosure is unauthorized, or otherwise knowingly violates these regulations, shall be subject to appropriate disciplinary action. GAO employees are prohibited from using personnel information not available to the public, obtained through official duties, for commercial solicitation or sale, or for personal gain. Any employee who knowingly violates this prohibition shall be subject to appropriate disciplinary action.

§ 83.9 Social Security number.

(a) GAO may not require individuals to disclose their Social Security Number (SSN) unless disclosure would be required—

(1) Under Federal statute; or

(2) Under any statute, executive order, or regulation that authorizes any Federal, State, or local agency maintaining a system of records that was in existence and operating prior to January 1, 1975, to request the SSN as a necessary means of verifying the identity of an individual.

(b) Individuals asked to voluntarily provide their SSN shall suffer no penalty or denial of benefits for refusing to provide it.

(c) When GAO requests an individual to disclose his or her SSN, it shall inform that individual whether that disclosure is mandatory or voluntary, by what statutory or other authority such number is solicited, and what uses will be made of it.

§ 83.10 First Amendment rights.

Personnel records or entries thereon describing how individuals exercise rights guaranteed by the First Amendment to the United States Constitution are prohibited, unless expressly authorized by statute or by the individual concerned, or unless pertinent to and within the scope of an authorized law enforcement activity. These rights include, but are not limited to, free exercise of religious and political beliefs, freedom of speech and the press, and freedom to assemble and to petition the Government.

§ 83.11 Official Personnel Folder.

(a) GAO shall establish and maintain an Official Personnel Folder for each of its employees, except as provided in the GAO/U.S. OPM/GSA Memorandum of Understanding (see subsection (b)). Except as provided for in Federal Personnel Manual (FPM) Supplement 293-31 there will be only one Official Personnel Folder maintained for each employee.

(b) *GAO/U.S. OPM/GSA Memorandum of Understanding.* The Memorandum of Understanding agreed to by the U.S. General Accounting Office, the U.S. Office of Personnel Management (U.S. OPM), and the National Archives and Records Service of the General Services Administration (GSA), Appendix I, constitutes the official and sole agreement concerning the continuity and coordination of the Official Personnel Folder.

(c) GAO policy is to assure continuity and coordination of the Official Personnel Folder when a person, for whom an Official Personnel Folder has been established, separates from GAO, or transfers to or from GAO from or to a Federal agency subject to regulations of the U.S. OPM relating to Official Personnel Folders. GAO will maximize the pooling of information between itself and those Federal agencies subject to U.S. OPM rules and regulations concerning the Official Personnel Folder so that a GAO employee may transfer to and from other Federal agencies with one complete and informative Official Personnel Folder.

(d) *Ownership of Official Personnel Folder.* (1) The Official Personnel Folders of individuals whose employment with GAO terminated prior to October 1, 1980, are the records of U.S. OPM and are under the jurisdiction and control of U.S. OPM.

(2) The Official Personnel Folders of current GAO employees whose GAO employment began on or after October 1, 1980, and who have had no previous employment by an executive branch agency of the Federal government shall be under the jurisdiction and control of, and are the records of GAO. GAO shall retain jurisdiction over such records even when they are transferred to an executive branch agency.

(3) The Official Personnel Folders of current GAO employees who were employed prior to October 1, 1980, by either GAO or an executive branch agency shall be under the control of GAO, but those records established

prior to October 1, 1980, by GAO, and all records established as a result of employment by an executive branch agency shall remain under the jurisdiction of, and be part of the records of, U.S. OPM.

(4) GAO will maintain those Official Personnel Folders containing records of employment by an executive branch Federal agency, or by GAO prior to October 1, 1980, in compliance with regulations of the U.S. OPM in accordance with the procedures contained in the Memorandum of Understanding and the provisions of regulations of U.S. OPM contained in 5 CFR Parts 293, 294, and 297, as well as the provisions of FPM Chapters 293, 294, and 297.

(e) *Maintenance and Content of Folder.* GAO shall maintain in the Official Personnel Folder the reports of selection and other personnel actions named in section 2951 of title 5, United States Code. The Folder shall also contain permanent records affecting the employee's status and service as required by U.S. OPM instructions and as designated in FPM Supplement 293-31.

(f) *Use of Existing Folders upon Transfer or Reemployment.* In accordance with paragraph (a) of this section, GAO shall request the transfer of the Official Personnel Folder for a person who was previously employed with a Federal agency that maintains such a Folder. The Folder so obtained shall be used in lieu of establishing a new Official Personnel Folder.

(1) When a person for whom an Official Personnel Folder has been established transfers from GAO to another Federal agency that maintains the Folder, GAO shall, on request, transfer the Folder to the new employing agency.

(2) Before transferring the Official Personnel Folder, GAO shall—

(i) Remove those records of a temporary nature filed on the left side of the Folder; and

(ii) Ensure that all permanent documents of the Folder are complete, correct, and present in the Folder in accordance with FPM Supplement 293-31.

(g) *Disposition of Folders of Former Federal Employees.* (1) Folders containing the personnel records of individuals separated from employment with GAO will be retained by GAO for 30 days after separation, and may be retained for an additional 60 days. Thereafter, the Folder shall be transferred to the same location and in the same manner as Official Personnel Folders of persons separated from Federal agencies which are subject to U.S. OPM regulations in accordance with the Memorandum of Understanding.

(2) GAO shall remove temporary records from the Folder before it is transferred in accordance with guidelines applicable to Federal agencies which are subject to U.S. OMP regulations.

(3) If a former GAO employee is reappointed in the Federal service, the employee's Folder shall, upon request, be transferred to the new employing agency.

(h) *Access Requests and Amendments to the Official Personnel Folder.* Requests for access to, disclosure from, correction of, or amendments to documents contained in the Official Personnel Folder will be made in accordance with the Memorandum of Understanding.

§ 83.12 Procedures for individual access to records.

(a) Upon written request by any individual outside of GAO or upon written or oral request by any officer or employee of GAO to gain access to his or her record or to any information pertaining to the individual which is contained in a system of personnel records, and not otherwise exempted, GAO shall permit the individual and upon the individual's request a person of his or her own choosing to accompany him or her, to review the record and have a copy made of all or any portion thereof in a form comprehensible to him or her, except that GAO may require the individual to furnish a written statement authorizing discussion of that individual's record in the accompanying person's presence. When access to the records has been granted by a system manager or designee:

(1) Inspection in person may be made in the office designated in the system notice during the hours specified by GAO.

(2) Upon the determination of the designated GAO official, records may be transferred to a GAO office more convenient to the data subject to review.

(3) Generally, GAO will not furnish certified copies of records. Where certified copies of records are to be furnished, they may be mailed at the request of the data subject or, as determined by GAO, only after payment of any fee levied in accordance with §83.17 is received.

(4) In no event shall original records be made available for review by the individual except in the presence of a system manager or designee.

(b) The general identifying information items that the designated GAO official may ask to be furnished before a specific inquiry is granted include:

(1) Full name, signature, and home address;

(2) Picture identification card;

(3) The current or last place and dates of Federal employment, if appropriate; and

(4) Social security number (for those systems of records retrieved by this identifier).

(c) A request or inquiry from someone other than the individual to whom the information pertains shall contain such documents or copies of documents that establish the relationship or authorize access as follows:

(1) When the requester is the parent or legal guardian of a data subject who is a minor, the requester shall identify the relationship with the data subject and furnish a certified or authenticated (e.g. notarized) copy of any document establishing parentage or appointment as legal guardian.

(2) Where the requester is the legal guardian of a data subject who has been declared incompetent by the courts, the requester shall identify the relationship with the data subject and furnish a certified or authenticated copy of the court's appointment of guardianship.

(3) Where the requester is a representative of the data subject, the requester shall identify the relationship with the data subject or the data subject's parent or legal guardian, and furnish documentation designating the representative as having the authority to act on behalf of the data subject.

(d) When the requester appears in person and cannot be identified by sight and signature, proof of identity is required as follows:

(1) When a request is from the data subject, the means of proof, in order of preference, are:

(i) A document bearing the individual's photograph and signature (for example, driver's license, passport, or military or civilian identification card); or

(ii) Two documents bearing the individual's signature (for example, Medicare card, unemployment insurance book, employer identification card, major credit card, professional, draft, or union membership card).

(2) When a request is made by the parent, legal guardian, or authorized representative of the data subject, the means of identifying the requester and his or her authority for acting on behalf of the data subject shall be as prescribed in paragraph (c) of this section. In addition, the requester shall establish the identity of the data subject by requiring the identifying information in paragraph (b) of this section.

(e) When a written inquiry or request is received from the data subject, or from the data subject's parent, legal guardian, or authorized representative, it should be signed and—

(1) For an inquiry, contain sufficient identifying information about the data subject to permit searching of the record system(s) and to permit response; and

(2) For an access request—

(i) From the data subject, contain sufficient information to locate the record and establish that the requester and the data subject are the same (e.g. matching signatures); or

(ii) From the data subject's parent, legal guardian, or authorized representative, contain sufficient information to locate the record, match identity with the data subject, and such documentation of association or authorization as is prescribed in paragraphs (c) and (d) of this section.

(f) The signed request from the data subject, or from the data subject's parent, legal guardian, or authorized representative specified in paragraph (c) of this section shall be sufficient proof of identity of the requester, unless for good cause, the system manager or designee determines that there is a need to require some notarized or certified evidence of the identity of the requester.

§ 83.13 Inquiries.

(a) General inquiries to request assistance in identifying which system of records may contain a record about an individual may be made in person or by mail to the Director, Personnel.

(b) An inquiry that requests GAO to determine if it has, in a given system of personnel records, a record about the inquirer, should be addressed to the official identified in the FEDERAL REGISTER notice for that system. Inquirers should specify the name of the system of personnel records, if known, as published in the FEDERAL REGISTER. Such inquiries should contain the identifying data prescribed in § 83.12 before a search can be made of that particular system of records.

§ 83.14 Denial of access requests.

(a) If an access request is denied, the official denying the request shall give the requester the following information:

(1) The official's name, position title, and business mailing address;

(2) The date of the denial;

(3) The reasons for the denial, including citation of appropriate sections of this or any other applicable part; and

(4) The individual's opportunities for further administrative consideration, including the name, position title, and address of the GAO official (see paragraph (c) of this section) responsible for such further review.

(b) Denial of a request for access to records will be made only by the official GAO designee and only upon a determination that:

(1) The record is subject to an exemption under § 83.21 when the system manager has elected to invoke the exemption; or

(2) The record is information compiled in reasonable anticipation of a civil action or proceeding; or

(3) The data subject or authorized representative of the data subject refuses to abide by procedures for gaining access to records.

(c) A request for administrative review of a denial shall be made to the Assistant Comptroller General for Human Resources, United States General Accounting Office, 441 G Street, NW, Washington, D.C. 20548. The Assistant Comptroller General shall acknowledge receipt of a request for administrative review of a denial of access within 10 working days after receipt of the request. If it is not possible to reach a decision within an additional 10 working days, the requester shall be informed of the approximate date (within 30 working days) when such a decision may be expected.

(d) In reaching a decision, the Assistant Comptroller General will review the criteria prescribed in this section which were cited as the basis for denying access, and may seek additional information as deemed necessary.

§ 83.15 Request for amendment of record.

(a) Individuals may request the amendment of their records in writing or in person by contacting the system manager or designee indicated in the notice of systems of records published by GAO in the FEDERAL REGISTER. Time limits will be measured from receipt at the proper office.

(b) A request for amendment should include the following:

(1) The precise identification of the records sought to be amended, deleted, or added.

(2) A statement of the reasons for the request, with all available documents and material that substantiate the request.

(c) GAO shall permit an individual to request amendment of a record pertaining to the individual. Not later than 10 working days after the date of receipt of such request, the designated GAO official shall acknowledge in writing such request and, promptly, either—

(1) Make any correction of any portion thereof which the individual believes is not accurate, relevant, timely, or complete; or

(2) Inform the individual of the refusal to amend the record in accordance with his or her request, the reason for the refusal, and the name and business address of the GAO official responsible for the refusal.

(3) The GAO offical shall permit an individual who disagrees with the refusal by the designated GAO official to amend his or her record to request review of such refusal. A request for administrative review of a denial shall be made in accordance with § 83.16.

(4) In any disclosure containing information about which the individual has filed a statement of disagreement, occurring after the filing of the statement under § 83.16(d), GAO shall clearly note any portion of the record which is disputed and provide copies of a concise statement of the reasons for not making the amendments requested, to persons or other agencies to whom the disputed record has been disclosed.

(5) Nothing in this section shall allow an individual access to any information compiled in reasonable anticipation of a civil action or proceeding.

(d) If necessary, the official authorized to rule on a request for amendment may seek additional information pertinent to the request to assure that a fair, equitable, and accurate decision is reached.

(e) The following criteria will be considered by the system manager or designee in reviewing initial requests for amendment of records:

(1) The sufficiency of the evidence submitted by the data subject;

(2) The factual accuracy of the information submitted and the information in the record;

(3) The relevancy, necessity, timeliness, and completeness of the information in light of the purpose for which it was collected;

(4) The degree of possibility that denial of the request could result in unfair determinations adverse to the data subject;

(5) The character of record sought to be amended;

(6) The propriety and feasibility of complying with specific means of amendment requested by the data subject; and

(7) The possible involvement of the record in a judicial or quasi-judicial process.

§ 83.16 Administrative review of request for amendment of record.

(a) A request for administrative review of GAO's denial to amend a record in GAO's system of personnel records shall be addressed to the Assistant Comptroller General for Human Resources, United States General Accounting Office, 441 G Street, NW, Washington, D.C. 20548. The Assistant Comptroller General shall acknowledge receipt of a request for administrative review of a denial of amendment within 10 working days.

(b) If a decision cannot be made within an additional 10-day period, a letter will be sent within that time explaining the delay and furnishing an expected date for the decision. A decision on the request must be made within 30 working days after receipt of the request. Only for good cause shown, and at the discretion of the Assistant Comptroller General for Human Resources can this time limit be extended. Any extension requires written notification to the requester explaining the reason for the extension and furnishing a new expected date for the decision. Generally, such extension shall be for no more than an additional 30 working days.

(c) When a request for administrative review of an amendment denial is submitted, the individual must provide a copy of the original request for amendment, a copy of the initial denial, and a statement of the specific reasons why the initial denial is believed to be in error.

(d) An individual requesting an amendment of a record has the burden of supplying information in support of the propriety and necessity of the amendment request. The decision on the request will then be rendered based on a review of the data submitted. The GAO official is not required to gather supporting evidence for the individual and will have the right to verify the evidence which the individual submits.

(e) Amendment of a record will be denied upon a determination by the system manager or designee that:

(1) The record is subject to an exemption from the provisions of this part, allowing amendment of records;

(2) The information submitted by the data subject is not accurate, relevant, or of sufficient probative value;

(3) The amendment would violate a statute or regulation;

(4) The individual refuses to provide information which is necessary to process the request to amend the record; or

(5) The record for which amendment is requested is a record presented in a judicial or quasi-judicial proceeding, or maintained in anticipation of being used in a judicial or quasi-judicial proceeding, when such record is or will become available to the individual under that proceeding.

(f) If, after review, the Assistant Comptroller General for Human Resources also refuses to amend the record in accordance with the request, the individual will be permitted to file with the system manager or designee of the system of records concerned a concise statement setting forth the reasons for his or her disagreement. Any such statement of disagreement will be treated in accordance with paragraph (c)(4) of § 83.15.

§ 83.17 Fees.

(a) Generally, GAO's policy is to provide the first copy of any record or portion thereof, furnished as a result of this part, at no cost to the data subject or authorized representative. However, in cases where GAO deems it appropriate (for example, where the record is voluminous), the system manager or designee in his or her discretion may charge a fee when the cost for copying the record (at a rate of 20 cents per page) would be in excess of ten dollars ($10).

(b) There shall be no fees charged or collected from a data subject for the following:

(1) Search for or retrieval of the data subject's records;

(2) Review of the records;

(3) Making a copy of a record when it is a necessary part of the process of making the record available for review;

(4) Copying at the initiative of GAO without a request from the individual;

(5) Transportation of the record; and

(6) Making a copy of an amended record to provide the individual with evidence of the amendment.

(c) Certification of authenticity shall be $10 for each certificate, which fee may be waived in the discretion of the system manager or designee.

§ 83.18 Rights of legal guardians.

For the purposes of this part, the parent of any minor, or the legal guardian of any individual who has been declared to be incompetent due to physical or mental incapacity or age by a court of competent jurisdiction, may act on behalf of the individual.

§ 83.19 Government contractors.

When GAO provides by a contract for the operation by or on behalf of GAO of a system of personnel records to accomplish a function of GAO, GAO shall, consistent with its authority, cause the requirements of this part to be applied to such system. Any such contractor and any employee of such contractor, if such contract is agreed to on or after the effective date of this section, shall be considered, for the purposes of this part, to be an employee of GAO. Contractor employees will be required to observe the confidentiality requirements of this part. Violations of this part by contractor employees may be a sufficient ground for contract termination.

§ 83.20 Mailing lists.

An individual's name and address may not be sold or rented by GAO unless such action is specifically authorized by law. This provision shall not be construed to require the withholding of names and addresses otherwise permitted to be made public.

§ 83.21 Exemptions.

(a) All personnel records are exempted from §§ 83.6(c), 83.12, 83.13, 83.14, and 83.15, relating to making an accounting of disclosures available to the data subject or his authorized representative and access to and amendment of the records and other sections relating to procedural requirements of the above-cited sections if the record is:

(1) Specifically authorized under criteria established by an Executive order to be kept secret in the interest of national defense or foreign policy and is in fact classified pursuant to such Executive order. *See* 31 U.S.C. 716(e)(1) and 718(b)(3) concerning the applicability of these requirements to GAO.

(2) Investigatory material compiled for law enforcement purposes: *Provided, however,* That if any individual is denied any right, privilege, or benefit that he would otherwise be entitled to by Federal law, or for which he would otherwise be eligible, as a result of the maintenance of such material, such material shall be provided to such individual, except to the extent that the disclosure of such material would reveal the identity of a source who furnished information to the Government under an express promise that the identity of the source would be held in confidence, or, prior to the effective date of this section, under an express or implied promise that the identity of the source would be held in confidence;

(3) Maintained in connection with providing protection services to the President of the United States or other individuals pursuant to section 3056 of Title 18, United States Code;

(4) Required by statute to be maintained and used solely as statistical records;

(5) Investigatory material compiled solely for the purposes of determining suitability, eligibility, or qualifications for Federal civilian employment, military service, Federal contracts, or access to classified information, but only to the extent that the disclosure of such material would reveal the identity of the source who furnished information to the Government under an express promise that the identity of the source would be held in confidence, or, prior to the effective date of this section, under an express or implied promise that the identity of the source would be held in confidence (*see* § 83.5(j)(1) for the procedure to be used to obtain investigative data originated by other Government agencies);

(6) Testing or examination material used solely to determine individual qualifications for appointment or promotion in the Federal service the disclosure of which would compromise the objectivity or fairness of the testing or examination process; or

(7) Evaluation material used to determine potential for promotion in the armed services, but only to the extent that the disclosure of such material would reveal the identity of a source who furnished information to the Government under an express promise that the identity of the source would be held in confidence, or, prior to the effective date of this section, under an express or implied promise that the identity of the source would be held in confidence.

APPENDIX I—MEMORANDUM OF UNDERSTANDING

This memorandum of understanding constitutes an agreement between the U.S. Office of Personnel Management (OPM), the National Archives and Records Service of the General Services Administration (NARS), and the U.S. General Accounting Office (GAO) concerning:

(1) The maintenance of the Official Personnel Folder (OPF) of an individual who has been employed in a position subject to the provisions of Title 5, U.S.C. and to the regulations and procedures issued by OPM to govern the Federal civil service, and also in a position subject to the GAO Personnel Act of 1980 (Pub. L. 96-191) and its implementing regulations and procedures;

(2) The exchange of personnel documents and data between the Federal civil service administered by OPM and the personnel system administered by GAO;

(3) The establishment of procedures for processing requests for access to, disclosure from, and amendment of documents in the OPF of an individual who has service under both personnel systems;

(4) The establishment of procedures to be followed by the National Personnel Records Center (NPRC) when responding to requests pertaining to separated employees in any of the following circumstances:

(a) When the OPF contains documentation resulting from employment in both systems;

(b) When a request is received for transfer of an OPF between systems;

(c) When processing a request for an OPF, and that OPF contains only records of GAO employment since October 1, 1980;

(5) The agreement of the parties to consult and cooperate in matters relating to the establishment and revision of personnel procedures which may have mutual effect so as to insure the sharing of essential information while minimizing the recordkeeping burden of all three parties.

SUBCHAPTER G—STANDARDS FOR WAIVER OF CLAIMS FOR ERRONEOUS PAYMENT OF PAY AND ALLOWANCES

PART 91—STANDARDS FOR WAIVER

Sec.
91.1 Prescription of standards.
91.2 Definitions.
91.3 Exclusions.
91.4 Waiver of claims for erroneous payment of pay and allowances.
91.5 Conditions for waiver of claims.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 5 U.S.C. 5584; 10 U.S.C. 2774; and 32 U.S.C. 716.

§ 91.1 Prescription of standards.

These regulations are issued by the Comptroller General of the United States in implementation of section 5584 of title 5, United States Code, as added by Pub. L. 90-616, approved October 21, 1968, as amended by Pub. L. 92-453, approved October 2, 1972, and Pub. L. 93-359, approved July 25, 1974, and also in implementation of new section 2774 added to Title 10, United States Code, and new section 716 added to Title 32, United States Code, by said Pub. L. 92-453. These regulations prescribe standards for the waiver of claims of the United States against a person arising out of an erroneous payment of pay or allowances to an employee of an agency and a member of the uniformed services, including the National Guard, the collection of which would be against equity and good conscience and not in the best interests of the United States.

[40 FR 36099, Aug. 19, 1975]

§ 91.2 Definitions.

In this subchapter:

(a) "Employee" means an employee as defined in 5 U.S.C. 2105 who is or was employed in a civilian capacity by an agency.

(b) "Agency" means—

(1) An executive agency as defined in 5 U.S.C. 105,

(2) The Government Printing Office,

(3) The Library of Congress,

(4) The Office of the Architect of the Capitol, and

(5) The Botanic Garden.

(c) "Pay" as it relates to an employee means salary, wages, pay, compensation, emoluments, and remuneration for services. It includes but is not limited to overtime pay; night, Sunday standby, irregular and hazardous duty differential; pay for Sunday and holiday work; payment for accumulated and accrued leave; and severance pay. It does not include travel and transportation expenses and allowances, and relocation allowances payable under 5 U.S.C. 5724a.

(d) "Allowances" as they relate to an employee include but are not limited to payments for quarters, uniforms, and overseas cost of living expenses, but exclude travel and transportation allowances, and relocation expenses payable under 5 U.S.C. 5724a.

(e) "Member" means a member or former member of the uniformed services, or member or former member of the National Guard.

(f) "Uniformed services" means the Army, Navy, Air Force, Marine Corps, Coast Guard, National Oceanic and Atmospheric Administration, and Public Health Service.

(g) "National Guard" means the Army National Guard, the Air National Guard, the Army National Guard of the United States, and Air National Guard of the United States.

(h) The term "Secretary concerned" is that as defined in section 101(5) of Title 37, United States Code.

(i) "Pay" as it relates to members includes but is not limited to base and longevity pay, basic pay, training duty pay, special and incentive pays, readjustment pay, severance pay, mustering-out pay, retainer pay, retired pay, retirement pay, lump sum leave pay, and equivalent pay. It does not include travel or transportation allowances.

(j) "Allowances" as they relate to members include but are not limited to payments in lieu of subsistence, quarters, uniforms, clothing, personal money allowance, family separation allowance, and overseas station allowance. They do not include travel or transportation allowances.

(k) "Aggregate amount" means gross entitlement due employee or member.

[37 FR 26095, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975]

§ 91.3 Exclusions.

This part does not apply to:

(a) Employees of the District of Columbia Government.

(b) Employees of the legislative branch of the Government except employees of the Architect of the Capitol, the Government Printing Office, the Library of Congress, the United States Botanic Garden, and the General Accounting Office.

(c) Employees of the Administrative Office of the U.S. Courts, the Federal Judicial Center and other employees of the judicial branch.

[37 FR 26095, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975]

§ 91.4 Waiver of claims for erroneous payment of pay and allowances.

(a) The Comptroller General of the United States may waive in whole or in part a claim of the United States in any amount arising out of erroneous payment or pay or allowances, to an employee or member when all of the conditions set out in § 91.5 are present. Claims referred to the Attorney General for litigation will not be considered for waiver by the Comptroller General of the United States without first having obtained permission from the Attorney General.

(b) The head of the agency or the Secretary concerned, as appropriate, may waive in whole or in part a claim of the United States in an amount aggregating not more than $500, without regard to any repayments, against any person arising out of an erroneous payment of pay or allowances to or on behalf of an employee or member when all of the conditions set out in § 91.5 are present, except that he may not waive such a claim which is the subject of an exception made by the Comptroller General in the account of any accountable official, or which has been transmitted to the General Accounting Office for collection or to the Attorney General for litigation. He may deny an application for waiver of a claim in any amount, provided that in those cases where the claim is in an amount aggregating more than $500 the employee or member must be advised of his right to appeal the denial to the Comptroller General of the United States.

[37 FR 26095, Dec. 8, 1972, as amended at 44 FR 18639, Mar. 29, 1979]

§ 91.5 Conditions for waiver of claims.

Claims of the United States arising out of an erroneous payment of pay or allowances may be waived in whole or in part in accordance with the provisions of § 91.4 whenever:

(a) The claim arises out of an erroneous payment of pay and allowances made to or in behalf of an employee on or after July 1, 1960, except that waiver action may not be taken (1) unless application is received either in the General Accounting Office or agency concerned within 3 years immediately following the date on which the erroneous payment of pay was discovered, or within 3 years after October 21, 1968, whichever is later, or (2) unless application is received either in the General Accounting Office or agency concerned within 3 years immediately following the date on which the erroneous payment of allowances was discovered, or October 2, 1975, whichever is later, or (3) in the case of employees of the Government Printing Office, the Library of Congress, the Office of the Architect of the Capitol, or the Botanic Garden unless application is received either in the General Accounting Office or in the office of the head of the agency concerned within 3 years immediately following the date on which the erroneous payment of pay or allowances was discovered or July 25, 1977, whichever is later.

(b) The claim arises out of an erroneous payment of pay or allowances made to or in behalf of a member except that waiver action may not be taken unless application is received either in the General Accounting Office or the office of the Secretary concerned within 3 years immediately following the date on which the erroneous payment of pay or allowances was discovered.

(c) Collection action under the claim would be against equity and good conscience and not in the best interests of the United States. Generally these criteria will be met by a finding that the erroneous payment of pay or allowances occurred through administrative error and that there is no indication of fraud, misrepresentation, fault or lack of good faith on the part of the employee or member or any other person having an interest in obtaining a waiver of the claim. Any significant unexplained increase in pay or allowances which would require a reasonable person to make inquiry concerning the correctness of his pay or allowances, ordinarily would preclude a waiver when the employee or member fails to bring the matter to the attention of appropriate officials. Waiver of overpayments of pay and allowances under this standard necessarily must depend upon the facts existing in the particular case. The facts upon which a waiver is based should be recorded in detail and made a part of the written record in accordance with the provisions of § 92.6 of this subchapter.

[37 FR 26095, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975]

PART 92—PROCEDURE

Sec.

92.1 Referral of applications for waiver or refund to the head of the agency or the Secretary concerned.
92.2 Investigation—Report of investigation.
92.3 Procedure of head of agency or Secretary concerned after receiving report of investigation.
92.4 Notification of waiver action.
92.5 Refund of amounts repaid and waived.
92.6 Written record.
92.7 Register of waivers—Report.
92.8 Referral of claims for collection or litigation.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 5 U.S.C. 5584, 10 U.S.C. 2774, and 32 U.S.C. 716.

§ 92.1 Referral of applications for waiver or refund to the head of the agency or the Secretary concerned.

All applications for waiver or refund shall be submitted to the head of the agency or the Secretary concerned of the department which made the erroneous payment of pay or allowances. Any such application which has not previously been considered for waiver shall be considered for waiver provided it was received within the time limitations of § 91.5 of this subchapter. In the absence of other request, either the Comptroller General of the United States, the Secretary concerned or the head of the agency which made the erroneous payment of pay or allowances may initiate the waiver procedure prescribed in these regulations.

[37 FR 26096, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975]

§ 92.2 Investigation—Report of investigation.

(a) Except as provided in paragraph (c) of this section, all claims of the United States considered for waiver shall be investigated by the agency which made the erroneous payment of pay or allowances.

(b) The report of investigation will be made to the head of the agency or the Secretary concerned and should include:

(1) A statement of the aggregate amount of the erroneous payment supported by a citation to the pay record or voucher or vouchers upon which the erroneous payment was made together with a showing as to the part of the erroneous payment made on each pay record or voucher.

(2) A statement showing the circumstances under which the erroneous payment was made, the date it was discovered and whether it was subject to an exception made by the Comptroller General of the United States.

(3) A statement as to whether there is any indication of fraud, misrepresentation fault, or lack of good faith on the part of the employee or member or any other person having an interest in obtaining a waiver of the claim.

(4) A statement by the employee or member as to his knowledge of the overpayment.

(5) Any other factual information in possession of the agency such as payroll change slips, personnel action forms, leave and earnings statements, indoctrination or other instruction indicating knowledge on the part of the employee or member concerning the possibility of having received an erroneous payment of pay or allowances.

(c) An investigation will not be required in those cases of overpayment of pay or allowances involving amounts of $100 or less where there is no indication in the record of fraud, misrepresentation, fault, or lack of good faith on the part of the employee or member or any other person having an interest in obtaining a waiver of the claim.

[37 FR 26096, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975; 47 FR 12607, Mar. 24, 1982]

§ 92.3 Procedure of head of agency or Secretary concerned after receiving report of investigation.

After the head of the executive agency or Secretary concerned receives the report of investigation made in accordance with the provisions of § 92.2 he shall:

(a) Determine the reason for the erroneous payment of pay and allowances, take such corrective action as may be required to prevent similar erroneous payments, and make a written report thereof (see § 92.6).

(b) Waive the claim of the United States in whole or in part without regard to any repayment, if it is in an amount aggregating not more than $500, and he determines that waiver would be proper, and record the date and reasons for the waiver, unless the claim has been referred to the Comptroller General for collection or the Attorney General for litigation in which case the report of investigation together with his recommendation will be referred to the Comptroller General of the United States. He may deny an application for waiver of a claim in any amount, provided that in those cases where the claim is in an amount aggregating more than $500 the employee or member must be advised of his right to appeal the denial to the Comptroller General of the United States.

(c) Refer the report of investigation to the Comptroller General of the United States for determination if he recommends waiver and the claim is in an amount aggregating more than $500, or

(d) Refer the report of investigation to the Comptroller General of the United States in any case in which he can take final action if he has doubt as to whether waiver action is proper, setting forth the basis for his doubt.

[37 FR 26096, Dec. 8, 1972, as amended at 44 FR 18639, Mar. 29, 1979]

§ 92.4 Notification of waiver action.

The Comptroller General of the United States or the head of the agency or the Secretary concerned, as the case may be, to the extent practicable, shall send written notification to all concerned as to the final action taken upon a claim of the United States for erroneous payment of pay and allowances considered for waiver. If he reasonably can be located, any person who has repaid to the United States all or part of a claim which has been waived in whole or in part and who has not previously made application for refund, in addition to being informed as to the waiver action shall also be informed of his right to make application to the employing agency or department concerned at the time of erroneous payment for refund within 2 years following the date of the waiver action.

[37 FR 26096, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975]

§ 92.5 Refund of amounts repaid and waived.

The employing agency or department concerned at the time of the erroneous payment shall refund any amounts to a person who has repaid to the United States all or part, as appropriate, of the claim which has been waived in whole or in part, to the extent waived, provided application is made to the employing agency or department concerned for the refund within 2 years following the date of the waiver. Refunds shall be charged to the appropriation from which the erroneous payment was made.

§ 92.6 Written record.

The report of investigation, a detailed account of the corrective action taken, an account of the waiver action taken and the reasons therefor, and other pertinent information such as the action taken upon an application for refund shall constitute the written record in each case.

[37 FR 26097, Dec. 8, 1972]

§ 92.7 Register of waivers—Report.

(a) Each agency or department concerned shall maintain a register, and where appropriate separate registers, one for employees and one for members, each register shall show the disposition of each claim of the United States for erroneous payment of pay and allowances considered for waiver. The registers, together with the written record as described in § 92.6, shall be available for review by the General Accounting Office.

(b) Within 60 days after the close of each fiscal year, the head of each agency or the Secretary concerned exercising waiver authority shall furnish a consolidated report to the Comptroller General of the United States showing the total amount waived by the agency including the number of waiver requests granted in full and the dollar amount waived; number of waiver requests denied in entirety and the amount thereof; number of claims which have been waived in part including the aggregate amount waived and the aggregate amount denied in this category; and the number of requests transmitted to the General Accounting Office for waiver action. There should also be furnished a report of the amount refunded as a result of waiver action by the head of the agency or Secretary concerned and the amount refunded as a result of waiver action by the Comptroller General.

[37 FR 26096, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975]

§ 92.8 Referral of claims for collection or litigation.

(a) If the head of the agency or Secretary concerned has considered waiver and has denied waiver in whole or in part he shall so advise the General Accounting Office when referral for collection is made to it pursuant to 31 U.S.C. 3702.

(b) No claim for the recovery of an erroneous payment of pay and allowances, which is under consideration for waiver shall be referred to the Attorney General unless the time remaining for suit within the applicable limitation does not permit such waiver consideration prior to referral.

[37 FR 26096, Dec. 8, 1972, as amended at 40 FR 36099, Aug. 19, 1975; 43 FR 56011, Nov. 30, 1978; 47 FR 56980, Dec. 22, 1982]

PART 93—EFFECT OF WAIVER

Sec.
93.1 Credit in accounts.
93.2 Waived payment deemed valid.
93.3 Effect on other authority.

AUTHORITY: 31 U.S.C. 711. Interpret or apply 5 U.S.C. 5584, 10 U.S.C. 2774, and 32 U.S.C. 716.

SOURCE: 37 FR 26097, Dec. 8, 1972, unless otherwise noted.

§ 93.1 Credit in accounts.

In the audit and settlement of the accounts of any accountable officer or official, full credit shall be given for any amounts with respect to which collection by the United States is waived.

§ 93.2 Waived payment deemed valid.

An erroneous payment of pay or allowances, the collection of which is waived is deemed a valid payment for all purposes.

§ 93.3 Effect on other authority.

The provisions of these regulations do not affect any authority under any statute, other than 5 U.S.C. 5584, 10 U.S.C. 2774 and 32 U.S.C. 716, to litigate, settle, compromise, or waive any claim of the United States.

CHAPTER II—FEDERAL CLAIMS COLLECTION STANDARDS (GENERAL ACCOUNTING OFFICE—DEPARTMENT OF JUSTICE)

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PART 101—SCOPE OF STANDARDS

Sec.

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AUTHORITY: 31 U.S.C. 3711.

SOURCE: 49 FR 8896, Mar. 9, 1984, unless otherwise noted.

§ 101.1 Prescription of standards.

The regulations in this chapter, issued jointly by the Comptroller General of the United States and the Attorney General of the United States under 31 U.S.C. 3711(e)(2), prescribe standards for the administrative collection, compromise, termination of agency collection, and the referral to the General Accounting Office, and to the Department of Justice for litigation, of civil claims as defined by 31 U.S.C. 3701(b), by the Federal Government for money or property. Additional guidance is contained in Title 4 of the General Accounting Office Policy and Procedures Manual for Guidance of Federal Agencies. Regulations prescribed by the head of an agency pursuant to 31 U.S.C. 3711(e)(1) will be reviewed by the General Accounting Office as a part of its audit of the agency's activities.

§ 101.2 Definitions.

(a) *Claim and debt.* For the purposes of these standards, the terms "claim" and "debt" are deemed synonymous and interchangeable. They refer to an amount of money or property which has been determined by an appropriate agency official to be owed to the United States from any person, organization, or entity, except another Federal agency.

(b) A debt is considered "delinquent" if it has not been paid by the date specified in the agency's initial written notification (§ 102.2 of this chapter) or applicable contractual agreement, unless other satisfactory payment arrangements have been made by that date, or if, at any time thereafter, the debtor fails to satisfy obligations under a payment agreement with the creditor agency.

(c) As used in this chapter, "referral for litigation" means referral to the Department of Justice for appropriate legal proceedings, unless the agency concerned has statutory authority for handling its own litigation.

(d) In this chapter, words in the plural form shall include the singular and vice versa; and words importing the masculine gender shall include the feminine and vice versa. The terms "includes" and "including" do not exclude matters not listed but which are in the same general class.

§ 101.3 Antitrust, fraud, tax, and interagency claims excluded.

(a) The standards in this chapter relating to compromise, suspension, and termination of collection action (Parts 103 and 104) do not apply to any claim based in whole or in part on conduct in violation of the antitrust laws, or to any claim as to which there is an indication of fraud, the presentation of a false claim, or misrepresentation on the part of the debtor or any other party having an interest in the claim. Only the Department of Justice has authority to compromise, suspend, or terminate collection action on such claims. The standards in this chapter relating to the administrative collection of claims (Part 102) do apply, but only to the extent authorized by the Department of Justice in a particular case. Upon identification of a claim of any of the types described in the first sentence of this paragraph, the agency involved should refer the matter promptly to the Department of Justice. At its discretion, the Department of Justice may return the claim to the forwarding agency for further handling in accordance with the regulations in this chapter.

(b) Tax claims, as to which differing exemptions, administrative considerations, enforcement considerations, and statutes apply, are also excluded from the coverage of this chapter.

(c) This chapter does not apply to claims between Federal agencies. Federal agencies should attempt to resolve interagency claims by negotiation. If the claim cannot be resolved by the agencies involved, it should be referred to the General Accounting Office.

§ 101.4 Compromise, waiver, or disposition under other statutes not precluded.

Nothing contained in this chapter is intended to preclude agency disposition of any claim under statutes and implementing regulations other than Subchapter II of Chapter 37 of Title 31 of the United States Code and these Standards, providing for the collection, compromise, termination of collection action, or waiver in whole or in part of such a claim. See, for example, the Federal Medical Care Recovery Act, 76 Stat. 593, 42 U.S.C. 2651 et seq., and applicable regulations, 28 CFR 43.1 et seq. In such cases, the laws and regulations which are specifically applicable to claims collection activities of a particular agency take precedence over this chapter. Except as provided in § 102.19 of this chapter (Exemptions), the standards set forth in this chapter should be followed in the disposition of civil claims by the Federal Government by collection, compromise, or termination of collection action (other than by waiver pursuant to other statutory authority) where neither the specific statute nor its implementing regulations establish standards governing such matters.

§ 101.5 Conversion claims.

The instructions contained in this chapter are directed primarily at the recovery of money on behalf of the United States and the circumstances in which Government claims may be disposed of for less than the full amount claimed. Nothing contained in this chapter is intended, however, to deter an agency from demanding the return of specific property or from demanding, in the alternative, either the return of the property or the payment of its value.

§ 101.6 Subdivision of claims not authorized.

Claims may not be subdivided to avoid the monetary ceiling established by 31 U.S.C. 3711(a)(2). A debtor's liability arising from a particular transaction or contract shall be considered a single claim in determining whether the claim is one of less than $20,000, exclusive of interest, penalties, and administrative costs, for purposes of compromise (§ 103.1 of this chapter) or suspension or termination of collection action (§ 104.1 of this chapter).

§ 101.7 Required administrative proceedings.

Nothing contained in this chapter is intended to require an agency to omit, foreclose, or duplicate administrative proceedings required by contract or other laws or regulations.

§ 101.8 Omissions not a defense.

The standards set forth in this chapter shall apply to the administrative handling of civil claims of the Federal Government for money or property but the failure of an agency to comply with any provision of this chapter shall not be available as a defense to any debtor.

PART 102—STANDARDS FOR THE ADMINISTRATIVE COLLECTION OF CLAIMS

Sec.
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Sec.
102.20 Additional administrative collection action.

Authority: Subchapter II of Chapter 37 of Title 31, U.S.C.

Source: 49 FR 8897, Mar. 9, 1984, unless otherwise noted.

§ 102.1 Aggressive agency collection action.

(a) Each Federal agency shall take aggressive action, on a timely basis with effective followup, to collect all claims of the United States for money or property arising out of the activities of, or referred to, that agency in accordance with the standards set forth in this chapter. However, nothing contained in this chapter is intended to require the General Accounting Office or the Department of Justice to duplicate collection actions previously undertaken by any other agency, or to perform collection actions which should have been undertaken by any other agency in accordance with the standards set forth in this chapter.

(b) All agencies are expected to cooperate with one another in their debt collection activities.

§ 102.2 Demand for payment.

(a) Appropriate written demands shall be made promptly upon a debtor of the United States in terms which inform the debtor of the consequences of failure to cooperate. A total of three progressively stronger written demands at not more than 30-day intervals will normally be made unless a response to the first or second demand indicates that a further demand would be futile and the debtor's response does not require rebuttal. In determining the timing of demand letters, agencies should give due regard to the need to act promptly so that, as a general rule, if necessary to refer the debt to the Department of Justice for litigation, such referral can be made within one year of the agency's final determination of the fact and the amount of the debt. When necessary to protect the Government's interests (for example, to prevent the statute of limitations, 28 U.S.C. 2415, from expiring), written demand may be preceded by other appropriate actions under this chapter, including immediate referral for litigation.

(b) The initial demand letter should inform the debtor of: (1) The basis for the indebtedness and whatever rights the debtor may have to seek review within the agency; (2) the applicable standards for assessing interest, penalties, and administrative costs (§ 102.13); and (3) the date by which payment is to be made, which normally should be not more than 30 days from the date that the initial demand letter was mailed or hand-delivered. Agencies should exercise care to insure that demand letters are mailed or hand-delivered on the same day that they are actually dated. Apart from this, there is no prescribed format for the demand letters. Agencies should utilize demand letters and procedures that will lead to the earliest practicable determination of whether the debt can be resolved administratively or must be referred for litigation.

(c) As appropriate to the circumstances, agencies may consider including, either in the initial demand letter or in subsequent letters, such items as the agency's willingness to discuss alternative methods of payment, policies with respect to use of consumer reporting agencies (§ 102.5) and collection services (§ 102.6), the agency's intentions with respect to referral of the debt to the Department of Justice for litigation, and, depending on applicable statutory authority, the debtor's entitlement to consideration of waiver.

(d) Agencies should respond promptly to communications from the debtor, within 30 days whenever feasible, and should advise debtors who dispute the debt to furnish available evidence to support their contentions.

(e) If, either prior to the initiation of, at any time during, or after completion of the demand cycle, an agency determines to pursue offset, then the procedures specified in §§ 102.3, 102.4, or 5 U.S.C. 5514, as applicable, should be followed. The availability of funds for offset and the agency's determination to pursue it release the agency from the necessity of further compliance with paragraphs (a), (b), and (c) of this section. If the agency has not already sent the first demand letter, the agency's written notification of its intent to offset must give the debtor the opportunity to make voluntary payment, a requirement which will be satisfied by compliance with the notice requirements of §§ 102.3, 102.4, or 5 U.S.C. 5514.

§ 102.3 Collection by administrative offset.

(a) Collection by administrative offset will be undertaken in accordance with these standards and implementing regulations established by each agency on all claims which are liquidated or certain in amount in every instance in which such collection is determined to be feasible and not otherwise prohibited.

(1) For purposes of this section, the term "administrative offset" has the meaning provided in 31 U.S.C. 3716(a)(1).

(2) Whether collection by administrative offset is feasible is a determination to be made by the creditor agency on a case-by-case basis, in the exercise of sound discretion. Agencies should consider not only whether administrative offset can be accomplished, both practically and legally, but also whether offset is best suited to further and protect all of the Government's interests. In appropriate circumstances, agencies may give due consideration to the debtor's financial condition, and are not required to use offset in every instance in which there is an available source of funds. Agencies may also consider whether offset would tend to substantially interfere with or defeat the purposes of the program authorizing the payments against which offset is contemplated. For example, under a grant program in which payments are made in advance of the grantee's performance, offset will normally be inappropriate. This concept generally does not apply, however, where payment is in the form of reimbursement.

(b) Except as provided in § 101.4, this paragraph or § 102.4, the standards in this paragraph shall apply to the collection of debts by administrative offset under 31 U.S.C. 3716, some other statutory authority, or the common law.

(1) Agencies shall prescribe regulations for the exercise of administrative offset.

(2) Agency regulations required by paragraph (b)(1) of this section shall establish procedures for providing a debtor, before the offset is made, with appropriate procedural rights. Except as otherwise required by law, those regulations shall provide for: Written notice of the nature and amount of the debt, and the agency's intention to collect by offset; opportunity to inspect and copy agency records pertaining to the debt; opportunity to obtain review within the agency of the determination of indebtedness; and opportunity to enter into a written agreement with the agency to repay the debt. Agency regulations shall also establish procedures for making requests for offset to other agencies holding funds payable to the debtor, and for processing requests for offset that are received from other agencies.

(i) Agencies have discretion and should exercise sound judgment in determining whether to accept a repayment agreement in lieu of offset. The determination should balance the Government's interest in collecting the debt against fairness to the debtor. If the debt is delinquent and the debtor has not disputed its existence or amount, an agency should accept a repayment agreement in lieu of offset only if the debtor is able to establish that offset would result in undue financial hardship or would be against equity and good conscience.

(ii) In cases where the procedural requirements specified in paragraph (b)(2) of this section have previously been provided to the debtor in connection with the same debt under some other statutory or regulatory authority, such as pursuant to a notice of audit disallowance, the agency is not required to duplicate those requirements before taking administrative offset.

(3) Agencies may not initiate administrative offset to collect a debt under 31 U.S.C. 3716 more than 10 years after the Government's right to collect the debt first accrued, unless facts material to the Government's right to collect the debt were not known and could not reasonably have been known by the official or officials of the Government who were charged with the responsibility to discover and collect

intent to offset must give the debtor the opportunity to make voluntary payment, a requirement which will be satisfied by compliance with the notice requirements of §§ 102.3, 102.4, or 5 U.S.C. 5514.

§ 102.3 Collection by administrative offset.

(a) Collection by administrative offset will be undertaken in accordance with these standards and implementing regulations established by each agency on all claims which are liquidated or certain in amount in every instance in which such collection is determined to be feasible and not otherwise prohibited.

(1) For purposes of this section, the term "administrative offset" has the meaning provided in 31 U.S.C. 3716(a)(1).

(2) Whether collection by administrative offset is feasible is a determination to be made by the creditor agency on a case-by-case basis, in the exercise of sound discretion. Agencies should consider not only whether administrative offset can be accomplished, both practically and legally, but also whether offset is best suited to further and protect all of the Government's interests. In appropriate circumstances, agencies may give due consideration to the debtor's financial condition, and are not required to use offset in every instance in which there is an available source of funds. Agencies may also consider whether offset would tend to substantially interfere with or defeat the purposes of the program authorizing the payments against which offset is contemplated. For example, under a grant program in which payments are made in advance of the grantee's performance, offset will normally be inappropriate. This concept generally does not apply, however, where payment is in the form of reimbursement.

(b) Except as provided in § 101.4, this paragraph or § 102.4, the standards in this paragraph shall apply to the collection of debts by administrative offset under 31 U.S.C. 3716, some other statutory authority, or the common law.

(1) Agencies shall prescribe regulations for the exercise of administrative offset.

(2) Agency regulations required by paragraph (b)(1) of this section shall establish procedures for providing a debtor, before the offset is made, with appropriate procedural rights. Except as otherwise required by law, those regulations shall provide for: Written notice of the nature and amount of the debt, and the agency's intention to collect by offset; opportunity to inspect and copy agency records pertaining to the debt; opportunity to obtain review within the agency of the determination of indebtedness; and opportunity to enter into a written agreement with the agency to repay the debt. Agency regulations shall also establish procedures for making requests for offset to other agencies holding funds payable to the debtor, and for processing requests for offset that are received from other agencies.

(i) Agencies have discretion and should exercise sound judgment in determining whether to accept a repayment agreement in lieu of offset. The determination should balance the Government's interest in collecting the debt against fairness to the debtor. If the debt is delinquent and the debtor has not disputed its existence or amount, an agency should accept a repayment agreement in lieu of offset only if the debtor is able to establish that offset would result in undue financial hardship or would be against equity and good conscience.

(ii) In cases where the procedural requirements specified in paragraph (b)(2) of this section have previously been provided to the debtor in connection with the same debt under some other statutory or regulatory authority, such as pursuant to a notice of audit disallowance, the agency is not required to duplicate those requirements before taking administrative offset.

(3) Agencies may not initiate administrative offset to collect a debt under 31 U.S.C. 3716 more than 10 years after the Government's right to collect the debt first accrued, unless facts material to the Government's right to collect the debt were not known and could not reasonably have been known by the official or officials of the Government who were charged with the responsibility to discover and collect

such debts. When the debt first accrued is to be determined according to existing law regarding the accrual of debts, such as under 28 U.S.C. 2415.

(4) Agencies are not authorized by 31 U.S.C. 3716 to use administrative offset with respect to: (i) Debts owed by any State or local Government; (ii) debts arising under or payments made under the Social Security Act, the Internal Revenue Code of 1954, or the tariff laws of the United States; or (iii) any case in which collection of the type of debt involved by administrative offset is explicitly provided for or prohibited by another statute. However, unless otherwise provided by contract or law, debts or payments which are not subject to administrative offset under 31 U.S.C. 3716 may be collected by administrative offset under the common law or other applicable statutory authority.

(5) Agencies may effect administrative offset against a payment to be made to a debtor prior to the completion of the procedures required by paragraph (b)(2) of this section if: (i) Failure to take the offset would substantially prejudice the Government's ability to collect the debt, and (ii) the time before the payment is to be made does not reasonably permit the completion of those procedures. Such prior offset must be promptly followed by the completion of those procedures. Amounts recovered by offset but later found not to be owed to the Government shall be promptly refunded.

(c) Type of hearing or review: (1) For purposes of this section, whenever an agency is required to afford a debtor with a hearing or review within the agency, the agency shall provide the debtor with a reasonable opportunity for an oral hearing when: (i) An applicable statute authorizes or requires the agency to consider waiver of the indebtedness involved, the debtor requests waiver of the indebtedness, and the waiver determination turns on an issue of credibility or veracity; or (ii) the debtor requests reconsideration of the debt and the agency determines that the question of the indebtedness cannot be resolved by review of the documentary evidence, for example, when the validity of the debt turns on an issue of credibility or veracity. Unless otherwise required by law, an oral hearing under this section is not required to be a formal evidentiary-type hearing, although the agency should always carefully document all significant matters discussed at the hearing.

(2) This section does not require an oral hearing with respect to debt collection systems in which determinations of indebtedness or waiver rarely involve issues of credibility or veracity and the agency has determined that review of the written record is ordinarily an adequate means to correct prior mistakes. In administering such a system, the agency is not required to sift through all of the requests received in order to accord oral hearings in those few cases which may involve issues of credibility or veracity.

(3) In those cases where an oral hearing is not required by this section, the agency shall nevertheless accord the debtor a "paper hearing," that is, the agency will make its determination on the request for waiver or reconsideration based upon a review of the written record.

(d) Appropriate use should be made of the cooperative efforts of other agencies in effecting collection by administrative offset, including use of the Army Holdup List. Generally, agencies should not refuse to comply with requests from other agencies to initiate administrative offset to collect debts owed to the United States, unless the requesting agency has not complied with the applicable provisions of these standards or the offset would be otherwise contrary to law.

(e) Collection by offset against a judgment obtained by a debtor against the United States shall be accomplished in accordance with 31 U.S.C. 3728.

(f) Whenever the creditor agency is not the agency which is responsible for making the payment against which administrative offset is sought, the latter agency shall not initiate the requested offset until it has been provided by the creditor agency with an appropriate written certification that the debtor owes a debt (including the amount) and that the provisions of this section have been fully complied with.

(g) When collecting multiple debts by administrative offset, agencies should apply the recovered amounts to those debts in accordance with the best interests of the United States, as determined by the facts and circumstances of the particular case, paying special attention to applicable statutes of limitations.

§ 102.4 Administrative offset against amounts payable from Civil Service Retirement and Disability Fund.

(a) Unless otherwise prohibited by law, agencies may request that moneys which are due and payable to a debtor from the Civil Service Retirement and Disability Fund be administratively offset in reasonable amounts in order to collect in one full payment or a minimal number of payments debts owed to the United States by the debtor. Such requests shall be made to the appropriate officials of the Office of Personnel Management in accordance with such regulations as may be prescribed by the Director of that Office.

(b) When making a request for administrative offset under paragraph (a) of this section, an agency shall include a written certification that:

(1) The debtor owes the United States a debt, including the amount of the debt;

(2) The requesting agency has complied with the applicable statutes, regulations, and procedures of the Office of Personnel Management; and

(3) The requesting agency has complied with the requirements of § 102.3 of this part, including any required hearing or review.

(c) Once an agency decides to request administrative offset under paragraph (a) of this section, it should make the request as soon as practical after completion of the applicable procedures in order that the Office of Personnel Management may identify and "flag" the debtor's account in anticipation of the time when the debtor requests or becomes eligible to receive payments from the Fund. This will satisfy any requirement that offset be initiated prior to expiration of the applicable statute of limitations. At such time as the debtor makes a claim for payments from the Fund, if at least a year has elapsed since the offset request was originally made, the debtor should be permitted to offer a satisfactory repayment plan in lieu of offset upon establishing that changed financial circumstances would render the offset unjust.

(d) If the requesting agency collects part or all of the debt by other means before deductions are made or completed pursuant to paragraph (a) of this section, the agency shall act promptly to modify or terminate its request for offset under paragraph (a) of this section.

(e) This section does not require or authorize the Office of Personnel Management to review the merits of the requesting agency's determination with respect to the amount and validity of the debt, its determination as to waiver under an applicable statute, or its determination to provide or not provide an oral hearing.

§ 102.5 Use of consumer reporting agencies.

(a) Agencies shall develop and implement procedures for reporting delinquent debts to consumer reporting agencies. For purposes of this section, the term "consumer reporting agency" has the meaning provided in 31 U.S.C. 3701(a)(3).

(b) In developing procedures under paragraph (a) of this section, agencies must have due regard for compliance with the Privacy Act of 1974, as amended, 5 U.S.C. 552a. However, consumer reporting agencies themselves are not subject to the Privacy Act.

(c) Agency procedures developed under paragraph (a) of this section shall be consistent with the requirements of 31 U.S.C. 3711(f) and § 102.3(c) of this part.

§ 102.6 Contracting for collection services.

(a) All agencies have authority to contract for collection services to recover delinquent debts, provided that the following conditions are satisfied:

(1) The authority to resolve disputes, compromise claims, suspend or terminate collection action, and refer the matter for litigation (§ 105.1) must be retained by the agency;

(2) The contractor shall be subject to the Privacy Act of 1974, as amended, to the extent specified in 5 U.S.C. 552a(m), and to applicable Federal and State laws and regulations pertaining to debt collection practices, such as the Fair Debt Collection Practices Act, 15 U.S.C. 1692;

(3) The contractor must be required to account strictly for all amounts collected; and

(4) The contractor must agree to provide any data contained in its files relating to paragraphs (a) (1), (2), and (3) of § 105.2 of this chapter upon returning an account to the creditor agency for subsequent referral to the Department of Justice for litigation.

(b) Funding of collection service contracts:

(1) An agency may fund a collection service contract on a fixed-fee basis, that is, payment of a fixed fee determined without regard to the amount actually collected under the contract. Payment of the fee under this type of contract must be charged to available agency appropriations.

(2) An agency may also fund a collection service contract on a contingent-fee basis, that is, by including a provision in the contract permitting the contractor to deduct its fee from amounts collected under the contract. The fee should be based on a percentage of the amount collected, consistent with prevailing commercial practice.

(3) An agency may enter into a contract under paragraph (b)(1) of this section only if and to the extent provided in advance in its appropriation act or other legislation, except that this requirement does not apply to the use of a revolving fund authorized by statute.

(4) Except as authorized under paragraph (b)(2) of this section, or unless otherwise specifically provided by law, agencies must deposit all amounts recovered under collection service contracts (or by agency employees on behalf of the agency) in the Treasury as miscellaneous receipts pursuant to 31 U.S.C. 3302.

§ 102.7 Personal interview with debtor.

Agencies will undertake personal interviews with their debtors whenever this is feasible, having regard for the amounts involved and the proximity of agency representatives to such debtors.

§ 102.8 Contact with debtor's employing agency.

When a debtor is employed by the Federal Government or is a member of the military establishment or the Coast Guard, and collection by offset cannot be accomplished in accordance with 5 U.S.C. 5514, the employing agency will be contacted for the purpose of arranging with the debtor for payment of the indebtedness by allotment or otherwise in accordance with section 206 of Executive Order No. 11222, May 8, 1965, 30 FR 6469.

§ 102.9 Suspension or revocation of license or eligibility.

Agencies seeking the collection of statutory penalties, forfeitures, or debts provided for as an enforcement aid or for compelling compliance should give serious consideration to the suspension or revocation of licenses or other privileges for any inexcusable, prolonged or repeated failure of a debtor to pay such a claim, and the debtor should be so advised. Any agency making, guaranteeing, insuring, acquiring, or participating in loans should give serious consideration to suspending or disqualifying any lender, contractor, broker, borrower or other debtor from doing further business with it or engaging in programs sponsored by it if such a debtor fails to pay its debts to the Government within a reasonable time, and the debtor should be so advised. The failure of any surety to honor its obligations in accordance with 31 U.S.C. 9305 is to be reported to the Treasury Department at once. Notification that a surety's certificate of authority to do business with the Federal Government has been revoked or forfeited by the Treasury Department will be forwarded by that Department to all interested agencies.

§ 102.10 Liquidation of collateral.

An agency holding security or collateral which may be liquidated and the proceeds applied on debts due it through the exercise of a power of sale in the security instrument or a nonjudicial foreclosure should do so by such procedures if the debtor fails to pay the debt within a reasonable time after demand, unless the cost of disposing of the collateral will be disproportionate to its value or special circumstances require judicial foreclosure. The agency should provide the debtor with reasonable notice of the sale, an accounting of any surplus proceeds, and any other procedures required by contract or law. Collection from other sources, including liquidation of security or collateral, is not a prerequisite to requiring payment by a surety or insurance concern unless such action is expressly required by statute or contract.

§ 102.11 Collection in installments.

(a) Whenever feasible, and except as otherwise provided by law, debts owed to the United States, together with interest, penalties, and administrative costs as required by § 102.13 of this part, should be collected in full in one lump sum. This is true whether the debt is being collected by administrative offset or by another method, including voluntary payment. However, if the debtor is financially unable to pay the indebtedness in one lump sum, payment may be accepted in regular installments. Agencies should obtain financial statements from debtors who represent that they are unable to pay the debt in one lump sum. Agencies which agree to accept payment in regular installments should obtain a legally enforceable written agreement from the debtor which specifies all of the terms of the arrangement and which contains a provision accelerating the debt in the event the debtor defaults. The size and frequency of installment payments should bear a reasonable relation to the size of the debt and the debtor's ability to pay. If possible, the installment payments should be sufficient in size and frequency to liquidate the Government's claim in not more than 3 years. Installment payments of less than $50 per month should be accepted only if justifiable on the grounds of financial hardship or for some other reasonable cause. An agency holding an unsecured claim for administrative collection should attempt to obtain an executed confess-judgment note, comparable to the Department of Justice Form USA-70a, from a debtor when the total amount of the deferred installments will exceed $750. Such notes may be sought when an unsecured obligation of a lesser amount is involved. When attempting to obtain confess-judgment notes, agencies should provide their debtors with written explanation of the consequences of signing the note, and should maintain documentation sufficient to demonstrate that the debtor has signed the note knowingly and voluntarily. Security for deferred payments other than a confess-judgment note may be accepted in appropriate cases. An agency may accept installment payments notwithstanding the refusal of a debtor to execute a confess-judgment note or to give other security, at the agency's option.

(b) If the debtor owes more than one debt and designates how a voluntary installment payment is to be applied as among those debts, that designation must be followed. If the debtor does not designate the application of the payment, agencies should apply payments to the various debts in accordance with the best interests of the United States, as determined by the facts and circumstances of the particular case, paying special attention to applicable statues of limitations.

§ 102.12 Exploration of compromise.

Agencies may attempt to effect compromise, preferably during the course of personal interviews, in accordance with the standards set forth in Part 103 of this chapter.

§ 102.13 Interest, penalties, and administrative costs.

(a) Except as provided in paragraphs (h) and (i) of this section, agencies shall assess interest, penalties, and administrative costs on debts owed to the United States pursuant to 31 U.S.C. 3717. Before assessing these charges, an agency must mail or hand-deliver a written notice to the debtor explaining the agency's requirements concerning the charges. (See § 102.2 of this part.)

(b) Interest shall accrue from the date on which notice of the debt and the interest requirements is first mailed or hand-delivered to the debtor (on or after October 25, 1982), using the most current address that is available to the agency. If an agency uses an "advance billing" procedure—that is, if it mails a bill before the debt is actually owed—it can include the required interest notification in the advance billing, but interest may not start to accrue before the debt is actually owed. Agencies should exercise care to insure that the notices required by this section are dated and mailed or hand-delivered on the same day.

(c) The rate of interest assessed shall be the rate of the current value of funds to the United States Treasury (*i.e.*, the Treasury tax and loan account rate), as prescribed and published by the Secretary of the Treasury in the FEDERAL REGISTER and the Treasury Fiscal Requirements Manual Bulletins annually or quarterly, in accordance with 31 U.S.C. 3717. An agency may assess a higher rate of interest if it reasonably determines that a higher rate is necessary to protect the interests of the United States. The rate of interest, as initially assessed, shall remain fixed for the duration of the indebtedness, except that where a debtor has defaulted on a repayment agreement and seeks to enter into a new agreement, the agency may set a new interest rate which reflects the current value of funds to the Treasury at the time the new agreement is executed. Interest should not be assessed on interest, penalties, or administrative costs required by this section. However, if the debtor defaults on a previous repayment agreement, charges which accrued but were not collected under the defaulted agreement shall be added to the principal to be paid under a new repayment agreement.

(d) An agency shall assess against a debtor charges to cover administrative costs incurred as a result of a delinquent debt,—that is, the additional costs incurred in processing and handling the debt because it became delinquent as defined in § 101.2(b) of this chapter. Calculation of administrative costs should be based upon actual costs incurred or upon cost analyses establishing an average of actual additional costs incurred by the agency in processing and handling claims against other debtors in similar stages of delinquency. Administrative costs may include costs incurred in obtaining a credit report or in using a private debt collector, to the extent they are attributable to delinquency.

(e) An agency shall assess a penalty charge, not to exceed 6 percent a year, on any portion of a debt that is delinquent as defined in § 101.2(b) of this chapter for more than 90 days. This charge need not be calculated until the 91st day of delinquency, but shall accrue from the date that the debt became delinquent.

(f) When a debt is paid in partial or installment payments, amounts received by the agency shall be applied first to outstanding penalty and administrative cost charges, second to accrued interest, and third to outstanding principal.

(g) An agency shall waive the collection of interest on the debt or any portion of the debt which is paid within 30 days after the date on which interest began to accrue. An agency may extend this 30-day period, on a case-by-case basis, if it reasonably determines that such action is appropriate. Also, an agency may waive, in whole or in part, the collection of interest, penalties, and/or administrative costs assessed under this section under the criteria specified in Part 103 of this chapter relating to the compromise of claims (without regard to the amount of the debt), or if the agency determines that collection of these charges would be against equity and good conscience or not in the best interests of the United States. Waiver under the first sentence of this paragraph (g) is mandatory. Under the second and third sentences, it may be exercised only in accordance with regulations issued by the agency identifying the standards and appropriate circumstances for waiver. Examples of situations which agencies may consider including in their interest waiver regulations are: (1) Waiver of interest pending consideration of a request for reconsideration, administrative review, or waiver of the underlying debt under a permissive statute, and (2) waiver of interest where the agency has accepted an installment plan under § 102.11 of this Part, there is no indication of fault or lack of good faith on the part of the debtor, and the amount of interest is large enough in relation to the size of the installments that the debtor can reasonably afford to pay that the debt will never be repaid.

(h) Where a mandatory waiver or review statute applies, interest and related charges may not be assessed for those periods during which collection action must be suspended under § 104.2(c)(1) of this chapter.

(i) *Exemptions.* (1) The provisions of 31 U.S.C. 3717 do not apply: (i) To debts owed by any State or local government; (ii) to debts arising under contracts which were executed prior to, and were in effect on (i.e., were not completed as of), October 25, 1982; (iii) to debts where an applicable statute, regulation required by statute, loan agreement, or contract either prohibits such charges or explicitly fixes the charges that apply to the debts involved; or (iv) to debts arising under the Social Security Act, the Internal Revenue Code of 1954, or the tariff laws of the United States.

(2) However, agencies are authorized to assess interest and related charges on debts which are not subject to 31 U.S.C. 3717 to the extent authorized under the common law or other applicable statutory authority.

§ 102.14 Analysis of costs.

Agency collection procedures should provide for periodic comparison of costs incurred and amounts collected. Data on costs and corresponding recovery rates for debts of different types and in various dollar ranges should be used to compare the cost effectiveness of alternative collection techniques, establish guidelines with respect to points at which costs of further collection efforts are likely to exceed recoveries, assist in evaluating offers in compromise, and establish minimum debt amounts below which collection efforts need not be taken. Cost and recovery data should also be useful in justifying adequate resources for an effective collection program, evaluating the feasibility and cost effectiveness of contracting for debt collection services under § 102.6, and determining appropriate charges for administrative costs under § 102.13(d).

§ 102.15 Documentation of administrative collection action.

All administrative collection action shall be documented and the bases for compromise, or for termination or suspension of collection action, should be set out in detail. Such documentation shall be retained in the appropriate claims file.

§ 102.16 Automation.

Agencies should automate their debt collection operations to the extent it is cost effective and feasible.

§ 102.17 Prevention of overpayments, delinquencies, and defaults.

Agencies should establish procedures to identify the causes of overpayments, delinquencies, and defaults and the corrective actions needed.

§ 102.18 Use and disclosure of mailing addresses.

(a) When attempting to locate a debtor in order to collect or compromise a debt under this chapter, an agency may send a written request to the Secretary of the Treasury (or designee) in order to obtain a debtor's mailing address from the records of the Internal Revenue Service.

(b) An agency may disclose a mailing address obtained under paragraph (a) of this section to other agents, including collection service contractors, in order to facilitate the collection or compromise of debts under this chapter, except that a mailing address may be disclosed to a consumer reporting agency only for the limited purpose of obtaining a commercial credit report on the particular taxpayer.

(c) Each agency shall ensure, by appropriate regulations and contract administration, that the agency and its agents, including consumer reporting agencies and collection service contractors, comply with the provisions of 26 U.S.C. 6103(p)(4) and applicable regulations of the Internal Revenue Service.

§ 102.19 Exemptions.

(a) The preceding sections of this part, to the extent they reflect remedies or procedures prescribed by the Debt Collection Act of 1982, such as administrative offset (§§ 102.3 and 102.4), use of consumer reporting agencies (§ 102.5), contracting for collection services (§ 102.6), and interest and related charges (§ 102.13), do not apply to debts arising under or payments made under the Internal Revenue Code of 1954, as amended (26 U.S.C. 1 *et seq.*), the Social Security Act (42 U.S.C. 301 *et seq.*), or the tariff laws of the United States. However, these remedies and procedures may still be authorized with respect to debts which are exempt from the purview of the Debt Collection Act of 1982, to the extent that they are authorized under some other statute or the common law.

(b) This section should not be construed as prohibiting use of these authorities or requirements when collecting debts owed by persons employed by agencies administering the laws cited in the preceding paragraph unless the debt "arose under" those laws.

§ 102.20 Additional administrative collection action.

Nothing contained in this chapter is intended to preclude the utilization of any other administrative remedy which may be available.

PART 103—STANDARDS FOR THE COMPROMISE OF CLAIMS

Sec.

103.1 Scope and application.
103.2 Inability to pay.
103.3 Litigative probabilities.
103.4 Cost of collecting claim.
103.5 Enforcement policy.
103.6 Joint and several liability.
103.7 Compromise for a combination of reasons.
103.8 Further review of compromise offers.
103.9 Restrictions.

AUTHORITY: 31 U.S.C. 3711.

SOURCE: 49 FR 8902, Mar. 9, 1984, unless otherwise noted.

§ 103.1 Scope and application.

(a) The standards set forth in this part apply to the compromise of claims pursuant to 31 U.S.C. 3711. The head of an agency may exercise such compromise authority with respect to claims for money or property arising out of the activities of that agency where the claim, exclusive of interest, penalties, and administrative costs, does not exceed $20,000, prior to the referral of such claims to the General Accounting Office, or to the Department of Justice for litigation. The Comptroller General may exercise such compromise authority with respect to claims referred to the General Accounting Office prior to their further referral for litigation. Only the Comptroller General may effect the compromise of a claim that arises out of an exception made by the General Accounting Office in the account of an accountable officer, including a claim against the payee, prior to its referral by that Office for litigation. Agency heads, including the Comptroller General, may designate officials within their respective agencies to exercise the authorities referred to in this section.

(b) When the claim, exclusive of interest, penalties, and administrative costs, exceeds $20,000, the authority to accept the compromise rests solely with the Department of Justice. The agency should evaluate the offer, using the factors set forth in this part. If the agency then wishes to accept the compromise, it must refer the matter to the Department of Justice, using the Claims Collection Litigation Report. See 4 CFR 105.2(b). Claims for which the gross amount is over $100,000 shall be referred to the Commercial Litigation Branch, Civil Division, Department of Justice, Washington, D.C. 20530. Claims for which the gross original amount is $100,000 or less shall be referred to the United States Attorney in whose judicial district the debtor can be found. The referral should specify the reasons for the agency's recommendation. Justice Department approval is not required if the agency wishes to reject the compromise offer.

§ 103.2 Inability to pay.

(a) A claim may be compromised pursuant to this Part if the Government cannot collect the full amount because of: (1) The debtor's inability to pay the full amount within a reasonable time, or (2) the refusal of the debtor to pay the claim in full and the Government's inability to enforce collection in full within a reasonable time by enforced collection proceedings.

(b) In determining the debtor's inability to pay, the following factors, among others, may be considered:

(1) Age and health of the debtor;

(2) Present and potential income;

(3) Inheritance prospects;

(4) The possibility that assets have been concealed or improperly transferred by the debtor; and

(5) The availability of assets or income which may be realized by enforced collection proceedings.

(c) The agency should give consideration to the applicable exemptions available to the debtor under State and Federal law in determining the Government's ability to enforce collection. Uncertainty as to the price which collateral or other property will bring at forced sale may properly be considered in determining the Government's ability to enforce collection. A compromise effected under this section should be for an amount which bears a reasonable relation to the amount which can be recovered by enforced collection procedures, having regard for the exemptions available to the debtor and the time which collection will take.

(d) Compromises payable in installments are to be discouraged. However, if payment of a compromise by installments is necessary, a legally enforceable agreement for the reinstatement of the prior indebtedness less sums paid thereon and acceleration of the balance due upon default in the payment of any installment should be obtained, together with security in the manner set forth in § 102.11 of this chapter, in every case in which this is possible.

(e) If the agency's files do not contain reasonably up-to-date credit information as a basis for assessing a compromise proposal, such information may be obtained from the individual debtor by obtaining a statement executed under penalty of perjury showing the debtor's assets and liabilities, income and expenses. Forms such as Department of Justice Form OBD-500 or OBD-500B may be used for this purpose. Similar data may be obtained from corporate debtors using a form such as Department of Justice Form OBD-500C or by resort to balance sheets and such additional data as seems required.

§ 103.3 Litigative probabilities.

A claim may be compromised pursuant to this Part if there is a real doubt concerning the Government's ability to prove its case in court for the full amount claimed, either because of the legal issues involved or a *bona fide* dispute as to the facts. The amount accepted in compromise in such cases should fairly reflect the probability of prevailing on the legal question involved, the probabilities with respect to full or partial recovery of a judgment, paying due regard to the availability of witnesses and other evidentiary support for the Government claim, and related pragmatic considerations. In determining the litigative risks involved, proportionate weight should be given to the probable amount of court costs and attorney fees pursuant to the Equal Access to Justice Act which may be assessed against the Government if it is unsuccessful in litigation. See 28 U.S.C. 2412.

§ 103.4 Cost of collecting claim.

A claim may be compromised pursuant to this part if the cost of collecting the claim does not justify the enforced collection of the full amount. The amount accepted in compromise in such cases may reflect an appropriate discount for the administrative and litigative costs of collection, paying heed to the time which it will take to effect collection. Costs of collecting may be a substantial factor in the settlement of small claims, but normally will not carry great weight in the settlement of large claims. In determining whether the cost of collecting justifies enforced collection of the full amount, it is legitimate to consider the positive effect that enforced collection of some claims may have on the collection of other claims. Since debtors are more likely to pay when first requested to do so if an agency has a policy of vigorous collection of all claims, the fact that the cost of collection of any one claim may exceed the amount of the claim does not necessarily mean that the claim should be compromised. The practical benefits of vigorous collection of a small claim may include a demonstration to other debtors that resistance to payment is not likely to succeed.

§ 103.5 Enforcement policy.

Statutory penalties, forfeitures, or debts established as an aid to enforcement and to compel compliance may be compromised pursuant to this part if the agency's enforcement policy in terms of deterrence and securing compliance, both present and future, will be adequately served by acceptance of the sum to be agreed upon. Mere accidential or technical violations may be dealt with less severely than willful and substantial violations.

§ 103.6 Joint and several liability.

When two or more debtors are jointly and severally liable, collection action will not be withheld against one such debtor until the other or others pay their proportionate shares. The agency should not attempt to allocate the burden of paying such claims as between the debtors but should proceed to liquidate the indebtedness as quickly as possible. Care should be taken that a compromise agreement with one such debtor does not release the agency's claim against the remaining debtors. The amount of a compromise with one such debtor shall not be considered a precedent or as morally binding in determining the amount which will be required from other debtors jointly and severally liable on the claim.

§ 103.7 Compromise for a combination of reasons.

A claim may be compromised for one or for more than one of the reasons authorized in this part.

§ 103.8 Further review of compromise offers.

If an agency holds a debtor's firm written offer of compromise which is substantial in amount and the agency is uncertain as to whether the offer should be accepted, it may refer the offer, the supporting data, and particulars concerning the claim to the General Accounting Office or to the Department of Justice. The General Accounting Office or the Department of Justice may act upon such an offer or return it to the agency with instructions or advice.

§ 103.9 Restrictions.

Neither a percentage of a debtor's profits nor stock in a debtor corporation will be accepted in compromise of a claim. In negotiating a compromise with a business concern, consideration should be given to requiring a waiver of the tax-loss-carry-forward and tax-loss-carry-back rights of the debtor.

PART 104—STANDARDS FOR SUSPENDING OR TERMINATING COLLECTION ACTION

Sec.
104.1 Scope and application.
104.2 Suspension of collection activity.
104.3 Termination of collection activity.
104.4 Transfer of claims.

AUTHORITY: 31 U.S.C. 3711(a)(3).

SOURCE: 49 FR 8903, Mar. 9, 1984, unless otherwise noted.

§ 104.1 Scope and application.

(a) The standards set forth in this part apply to the suspension or termination of collection action pursuant to 31 U.S.C. 3711(a)(3) on claims which do not exceed $20,000, exclusive of interest, penalties, and administrative costs, after deducting the amount of partial payments or collections, if any. The head of an agency (or designee) may suspend or terminate collection action under this part with respect to claims for money or property arising out of activities of that agency prior to the referral of such claims to the General Accounting Office or to the Department of Justice for litigation. The Comptroller General (or designee) may exercise such authority with respect to claims referred to the General Accounting Office prior to their further referral for litigation.

(b) If, after deducting the amount of partial payments or collections, if any, a claim exceeds $20,000, exclusive of interest, penalties, and administrative costs, the authority to suspend or terminate rests solely with the Department of Justice. If the agency thinks suspension or termination may be appropriate, it should evaluate the matter, using the factors set forth in this part. If the agency then concludes that suspension or termination is appropriate, it must refer the matter to the Department of Justice, using the Claims Collection Litigation Report. See 4 CFR § 105.2(b). The referral should specify the reasons for the agency's recommendation. If the agency decides not to suspend or terminate collection action on the claim, Justice Department approval is not required. If an agency determines that its claim is plainly erroneous or clearly without legal merit, it may terminate collection action regardless of the amount involved, without the need for Department of Justice concurrence.

§ 104.2 Suspension of collection activity.

(a) *Inability to locate debtor.* Collection action may be suspended temporarily on a claim when the debtor cannot be located after diligent effort and there is reason to believe that future collection action may be sufficiently productive to justify periodic review and action on the claim, with due consideration for the size and amount which may be realized thereon. The following sources may be of assistance in locating missing debtors: Telephone directories; city directories; postmasters; drivers' license records; automobile title and registration records; state and local governmental agencies; the Internal Revenue Service (§ 102.18 of this chapter); other Federal agencies; employers, relatives, friends; credit agency skip locate reports, and credit bureaus. Suspension as to a particular debtor should not defer the early liquidation of security for the debt. Every reasonable effort should be made to locate missing debtors sufficiently in advance of the bar of the applicable statute of limitations, such as 28 U.S.C. 2415, to permit the timely filing of suit if such action is warranted. If the missing debtor has signed a confess-judgment note and is in default, referral of the note for the entry of judgment should not be delayed because of the debtor's missing status.

(b) *Financial condition of debtor.* Collection action may also be suspended temporarily on a claim when the debtor owns no substantial equity in realty or personal property and is unable to make payments on the Government's claim or effect a compromise at the time but the debtor's future prospects justify retention of the claim for periodic review and action, and:

(1) The applicable statute of limitations has been tolled or started running anew; or

(2) Future collection can be effected by offset, notwithstanding the statute of limitations, with due regard to the 10-year limitation prescribed by 31 U.S.C. 3716(c)(1); or

(3) The debtor agrees to pay interest on the amount of the debt on which collection action will be temporarily suspended, and such temporary suspension is likely to enhance the debtor's ability to fully pay the principal amount of the debt with interest at a later date.

(c) *Request for waiver or administrative review.* (1) If the statute under which waiver or administrative review is sought is "mandatory," that is, if it prohibits the agency from collecting the debt prior to the agency's consideration of the request for waiver or review (see *Califano* v. *Yamasaki*, 422 U.S. 682 (1979)), then collection action must be suspended until either: (i) The agency has considered the request for waiver/review, or (ii) the applicable time limit for making the waiver/review request, as prescribed in the agency's regulations, has expired and the debtor, upon proper notice, has not made such a request.

(2) If the applicable waiver/review statute is "permissive," that is, if it does not require all requests for waiver/review to be considered, and if it does not prohibit collection action pending consideration of a waiver/review request (for example, 5 U.S.C.

5584), collection action may be suspended pending agency action on a waiver/review request based upon appropriate consideration, on a case-by-case basis, as to whether:

(i) There is a reasonable possibility that waiver will be granted, or that the debt (in whole or in part) will be found not owing from the debtor;

(ii) The Government's interests would be protected, if suspension were granted, by reasonable assurance that the debt could be recovered if the debtor does not prevail; and

(iii) Collection of the debt will cause undue hardship.

(3) If the applicable statutes and regulations would not authorize refund by the agency to the debtor of amounts collected prior to agency consideration of the debtor's waiver/review request in the event the agency acts favorably on it, collection action should ordinarily be suspended, without regard to the factors specified in paragraph (c)(2) of this section, unless it appears clear, based on the request and the surrounding circumstances, that the request is frivolous and was made primarily to delay collection.

§ 104.3 Termination of collection activity.

The head of an agency (or designee) may terminate collection activity and consider the agency's file on the claim closed under the following standards:

(a) *Inability to collect any substantial amount.* Collection action may be terminated on a claim when it becomes clear that the Government cannot collect or enforce collection of any significant sum from the debtor, having due regard for the judicial remedies available to the Government, the debtor's future financial prospects, and the exemptions available to the debtor under State and Federal law. In determining the debtor's inability to pay, the following factors, among others, may be considered: Age and health of the debtor; present and potential income; inheritance prospects; the possibility that assets have been concealed or improperly transferred by the debtor; the availability of assets or income which may be realized by enforced collection proceedings.

(b) *Inability to locate debtor.* Collection action may be terminated on a claim when the debtor cannot be located, and either: (1) There is no security remaining to be liquidated, or (2) the applicable statute of limitations has run and the prospects of collecting by offset, notwithstanding the bar of the statute of limitations, are too remote to justify retention of the claim.

(c) *Cost will exceed recovery.* Collection action may be terminated on a claim when it is likely that the cost of further collection action will exceed the amount recoverable thereby.

(d) *Claim legally without merit.* Collection action should be terminated immediately on a claim whenever it is determined that the claim is legally without merit.

(e) *Claim cannot be substantiated by evidence.* Collection action should be terminated when it is determined that the evidence necessary to prove the claim cannot be produced or the necessary witnesses are unavailable and efforts to induce voluntary payment are unavailing.

§ 104.4 Transfer of claims.

When an agency has doubt as to whether collection action should be suspended or terminated on a claim, it may refer the claim to the General Accounting Office for advice. When a significant enforcement policy is involved in reducing a statutory penalty or forfeiture to judgment, or recovery of a judgment is a prerequisite to the imposition of administrative sanctions, such as the suspension or revocation of a license or the privilege of participating in a Government sponsored program, an agency may refer such a claim for litigation even though termination of collection activity might otherwise be given consideration under § 104.3 (a) or (c). Claims on which an agency holds a judgment by assignment or otherwise will be referred to the Department of Justice for further action if renewal of the judgment lien or enforced collection proceedings are justified under the criteria discussed in this part, unless the agency concerned has statutory authority for handling its own litigation.

PART 105—REFERRALS TO DEPARTMENT OF JUSTICE OR GAO

Sec.
105.1 Prompt referral.
105.2 Claims collection litigation report.
105.3 Preservation of evidence.
105.4 Minimum amount of referrals to Department of Justice.
105.5 Preliminary referrals to GAO.

AUTHORITY: 31 U.S.C. 3711.

SOURCE: 49 FR 8904, Mar. 9, 1984, unless otherwise noted.

§ 105.1 Prompt referral.

(a) Except as provided in paragraphs (b) and (c) of this section, claims on which aggressive collection action has been taken in accordance with Part 102 of this chapter and which cannot be compromised, or on which collection action cannot be suspended or terminated, in accordance with Parts 103 and 104 of this chapter, shall be promptly referred to the Department of Justice for litigation. Claims for which the gross original amount is over $100,000 shall be referred to the Commercial Litigation Branch, Civil Division, Department of Justice, Washington, D.C. 20530. Claims for which the gross original amount is $100,000 or less shall be referred to the United States Attorney in whose judicial district the debtor can be found. Referrals should be made as early as possible, consistent with aggressive agency collection action and the observance of the regulations contained in this chapter, and in any event, well within the period for bringing a timely suit against the debtor. Ordinarily, referrals should be made within one year of the agency's final determination of the fact and the amount of the debt.

(b) Claims arising from audit exceptions taken by the General Accounting Office to payments made by agencies must be referred to the General Accounting Office for review and approval prior to referral to the Department of Justice for litigation, unless the agency concerned has been granted an exception by the General Accounting Office.

(c) When the merits of the Government's claim, the amount owed on the claim, or the propriety of acceptance of a proposed compromise, suspension, or termination are in doubt, the agency concerned should refer the matter to the General Accounting Office for resolution and instructions prior to proceeding with collection action and/or referral to the Department of Justice for litigation.

(d) Once a claim has been referred to GAO or to the Department of Justice pursuant to this section, the referring agency shall refrain from having any contact with the debtor and shall direct the debtor to GAO or the Department of Justice, as appropriate, when questions concerning the claim are raised by the debtor. GAO or the Department of Justice, as appropriate, shall be immediately notified by the referring agency of any payments which are received from the debtor subsequent to referral of a claim under this section.

§ 105.2 Claims collection litigation report.

(a) Unless an exception has been granted by the Department of Justice in consultation with the General Accounting Office, the Claims Collection Litigation Report (CCLR), which was officially implemented by the General Accounting Office on January 20, 1983, shall be used with all referrals of administratively uncollectible claims made pursuant to § 105.1. As required by the CCLR, the following information shall be included.

(1) *Report of prior collection actions.* A checklist or brief summary of the actions previously taken to collect or compromise the claim will be forwarded with the claim upon its referral. If any of the administrative collection actions enumerated in Part 102 of this chapter have been omitted, the reason for their omission must be provided. GAO, the United States Attorney, or the Civil Division of the Department of Justice may return claims at their option when there is insufficient justification for the omission of one or more of the administrative collection actions enumerated in Part 102 of this chapter.

(2) *Current address of debtor.* The current address of the debtor, or the name and address of the agent for a corporation upon whom service may

be made shall be provided. Reasonable and appropriate steps will be taken to locate missing parties in all cases. Referrals to the Department of Justice for the institution of foreclosure or other proceedings, in which the current address of any party is unknown, will be accompanied by a listing of the prior known addresses of such party and a statement of the steps taken to locate that party.

(3) *Credit data.* Reasonably current credit data indicating that there is a reasonable prospect of effecting enforced collection from the debtor, having due regard for the exemptions available to the debtor under State and Federal law and the judicial remedies available to the Government, shall be included.

(i) Such credit data may take the form of: (A) A commercial credit report; (B) an agency investigative report showing the debtor's assets, liabilities, income, and expenses; (C) the individual debtor's own financial statement executed under penalty of perjury reflecting the debtor's assets, liabilities, income, and expenses; or (D) an audited balance sheet of a corporate debtor.

(ii) Such credit data may be omitted if: (A) A surety bond is available in an amount sufficient to satisfy the claim in full; (B) the forced sale value of the security available for application to the Government's claim is sufficient to satisfy the claim in full; (C) the referring agency wishes to liquidate loan collateral through judicial foreclosure but does not desire a deficiency judgment; (D) the debtor is in bankruptcy or receivership; (E) the debtor's liability to the Government is fully covered by insurance, in which case the agency will furnish such information as it can develop concerning the identity and address of the insurer and the type and amount of insurance coverage; or (F) the nature of the debtor is such that credit data is not normally available or cannot reasonably be obtained, for example, a unit of State or local government.

(b) Agencies shall also use the CCLR when referring claims to the Department of Justice in order to obtain the approval of that Department with respect to compromise, suspension, or termination, as required by §§ 103.1(b) and 104.1(b).

§ 105.3 Preservation of evidence.

Care will be taken to preserve all files, records, and exhibits on claims referred or to be referred to the Department of Justice for litigation. Under no circumstances should original documents be sent to the Department of Justice or to the United States Attorney without specific prior approval to do so. Copies of relevant documents should be sent whenever necessary.

§ 105.4 Minimum amount of referrals to Department of Justice.

Agencies will not refer claims of less than $600, exclusive of interest, penalties, and administrative costs, for litigation unless: (a) Referral is important to a significant enforcement policy, or (b) the debtor not only has the clear ability to pay the claim but the Government can effectively enforce payment, having due regard for the exemptions available to the debtor under State and Federal law and the judicial remedies available to the Government.

§ 105.5 Preliminary referrals to GAO.

Preliminary referrals of claims to the General Accounting Office, as required by § 105.1(b) and (c), will be in accordance with instructions, including monetary limitations, contained in the General Accounting Office Policy and Procedures Manual for Guidance of Federal Agencies, and the provisions of §§ 105.2 and 105.3 of this part.

CHAPTER III—GENERAL ACCOUNTING OFFICE (CASB)

Editorial Note: For the benefit of CFR users, this edition of 4 CFR Chapter III includes a special feature, the preambles to Parts 331, 332, 351, and 400-420 of the regulations of the Cost Accounting Standards Board. The inclusion of the preambles is a joint effort by the Office of the Federal Register and the Cost Accounting Standards Board to provide readers with the administrative history of the regulations. The preambles appear as originally published in the daily Federal Register, in supplements to their respective parts. Further explanatory notes are printed immediately after the table of contents to each part.

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SUBCHAPTER A—ADMINISTRATION

PART 301—GENERAL INFORMATION AND ORGANIZATION

Subpart A—Organization

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Authority: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

Source: 36 FR 23916, Dec. 16, 1971, unless otherwise noted.

Subpart A—Organization

§ 301.1 Purpose.

This part together with Part 303, Release of Information, and Part 304, Delegations, of this chapter is published in compliance with Pub. L. 90-23, section (a)(1), 5 U.S.C. 552(a)(1), and constitutes a description of the Cost Accounting Standards Board.

§ 301.2 General statement of the Board's functions.

In general, the Board promulgates cost accounting standards designed to achieve uniformity and consistency in the cost accounting practices followed by defense contractors. It also promulgates rules and regulations for the implementation of such standards.

§ 301.3 Methods.

In carrying out its functions, the Cost Accounting Standards Board utilizes the following methods.

(a) The Board employs a staff consisting of various specialists dealing with particular areas of administrative and technical work, who advise the Board and perform duties assigned to them or which have been specifically delegated to them.

(b) Rules are published in the Federal Register and codified in this Title 4 of the Code of Federal Regulations. These rules may be inspected in the Board's offices or purchased from the Superintendent of Documents, Government Printing Office. The published rules include:

(1) Procedural regulations which govern the formal and informal methods whereby persons dealing with the Board can present information to the Board to enable the Board to promulgate rules, regulations, and cost accounting standards and to perform other duties for which it is responsible under section 719 of the Defense Production Act of 1950, as amended (50 U.S.C. App. 2168).

(2) Rules, regulations, and cost accounting standards which prescribe for relevant Federal agencies and for defense contractors and subcontractors various substantive and procedural requirements relating to cost accounting standards for use in connection with defense contracts.

(3) Regulations delegating matters to the Board's staff and describing how the public may deal with the Board in obtaining information.

(4) Board bylaws which govern Board membership, meetings, and formal action by Board vote.

(c) The Board may at its discretion respond to requests for interpretation of its rules, regulations, and cost accounting standards.

§ 301.4 Offices.

The Cost Accounting Standards Board's offices are located in the General Accounting Office Building, 441 G Street NW., Washington, DC 20548. The hours of business for the Board are 8:30 a.m. to 5 p.m., local time, Monday through Friday, excluding holidays observed by the Federal Government in Washington, D.C.

§ 301.5 Views and comments.

Proposed rules, regulations, or cost accounting standards of the Cost Accounting Standards Board shall be published for comment in the Federal Register. All parties affected thereby shall be afforded a period of not less than 30 days in which to submit to the Board their views and comments on the proposal; but in exceptional cases, the Board may provide for fewer than 30 days for the submission of views and comments. When fewer than 30 days are allowed, the Board notice inviting views and comments shall state the reasons therefor.

§ 301.6 Public hearings.

Public hearings to assist the Board in developing its rules, regulations, and cost accounting standards may be held to the extent the Board in its sole discretion deems desirable. Notices of such hearings shall be given by publication in the FEDERAL REGISTER.

§ 301.7 Formal submission.

All formal submissions required or permitted to be made to the Board under the rules, regulations, or cost accounting standards should be addressed to the Cost Accounting Standards Board, 441 G Street NW., Washington, DC 20548, in an original and two copies, unless otherwise provided by the rule, regulation, or standard under which submission is made. Where no form requirement is there specified, submission in letter or other reasonable form will be accepted.

§ 301.8 Final publication.

Any proposed rule, regulation, or cost accounting standard required to be published under section 719(i)(A) of the Defense Production Act of 1950, as amended, 50 U.S.C. App. 2168(i)(A), shall be published in the FEDERAL REGISTER after the Board has considered views and comments submitted pursuant to § 301.5 and any public hearing held pursuant to § 301.6.

§ 301.9 Transmittal to the Congress.

Transmittal to the Congress of any proposed rule, regulation, or cost accounting standard as required by section 719(h)(3) of the Defense Production Act of 1950, as amended, 50 U.S.C. App. 2168(h)(3), shall be made simultaneously with final publication of the proposed rule, regulation, or cost accounting standard as provided for in § 301.8.

§ 301.10 Organization and delegation of authority.

The Board, consisting of the Comptroller General of the United States who is the Chairman and four Board members appointed by him for terms of 4 years, acts to carry out the duties and responsibilities of the Cost Accounting Standards Board, established by Pub. L. 91-379, 84 Stat. 796, 50 U.S.C. App. 2166, 2168. The Board's staff of professional, technical, and supporting personnel is directed and supervised by the Executive Secretary. Delegations of authority to the Executive Secretary and other staff members are described in detail in Part 304 of this Title 4.

§ 301.11 Availability of information and materials.

The Board publishes a regulation in 4 CFR Part 303 concerning the availability for inspection and copying of Board records. That regulation states in detail what information is available, and what and where records may be inspected. Generally speaking, the following records are maintained and available.

(a) Minutes of Board meetings.

(b) Substantive regulations of general applicability and general policy and interpretation of general applicability.

(c) Rules, regulations, and cost accounting standards issued pursuant to section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C. App. 2168.

(d) A record of every Board proceeding including the final votes of each member of the Board participating in the proceeding.

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AUTHORITY: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

SOURCE: 36 FR 23917, Dec. 16, 1971, unless otherwise noted.

Subpart A—General Provisions

§ 302.1 Purpose.

The Government service requires the maintenance of unusually high standards of honesty, integrity, impartiality, and conduct by Government employees and special Government employees to assure the proper performance of Government business and the maintenance of confidence by citizens in their Government. This is especially true of service in the Cost Accounting Standards Board because of the unique functions and special trust placed upon the Board as an agent of the Congress. Board members, employees, and special Government employees are, therefore, expected and required to exercise informed judgments to avoid misconduct and conflicts of interest and the appearance of conflicts of interest. In accordance with these concepts, this regulation sets forth the regulations and policies of the Cost Accounting Standards Board which prescribe standards of conduct and responsibilities including guidance on conflict of interest laws and the requirement for reporting employment and financial interests for its Board members, employees, and special Government employees.

§ 302.2 Definitions.

In this regulation:

(a) Board means the Cost Accounting Standards Board, established by section 719 of the Defense Production Act of 1950, as amended, added by section 103 of Pub. L. 91-379, 84 Stat. 795.

(b) Chairman means the Comptroller General of the United States or, in the event of the absence or incapacity of the Comptroller General or during a vacancy in the office, the official of the General Accounting Office acting as Comptroller General.

(c) Board member means the Chairman and a person appointed by him pursuant to section 719(a) of Pub. L. 91-379.

(d) Executive Secretary means the employee appointed by the Board as Executive Secretary pursuant to section 719(b) of Pub. L. 91-379, or in the event of the absence or incapacity of the Executive Secretary or during a vacancy in that position, the employee delegated or designated to act as Executive Secretary.

(e) Employee means an officer or employee of the Board other than a special Government employee.

(f) Special Government employee means an officer or employee who is retained, designated, appointed, or employed to perform, with or without compensation, for a period not to exceed 130 days during any period of 365 days, temporary duties for the Board either on a full-time or intermittent basis (18 U.S.C. 202).

(g) Person means an individual, a corporation, a company, an association, a firm, a partnership, a society, a joint stock company, or any other organization or institution.

(h) Former employee means a former Board employee or former special Government employee of the Board, as defined in paragraph (f) of this section.

(i) Words importing the masculine gender include the feminine as well, and words importing the plural include the singular.

§ 302.3 Interpretation and advisory service.

The Executive Secretary, with the approval of the Chairman shall designate a Counselor for the Board who shall be responsible for providing counseling services and authoritative advice and guidance to Board members, employees, and special Government employees who seek advice and guidance from him on conflicts of interest questions.

§ 302.4 Compliance.

(a) The Chairman shall be responsible for seeing to it that this regulation is fully complied with and for issuing whatever supplementary instructions are deemed desirable. Except as otherwise specifically provided for in this regulation, any matter coming within the provisions of this regulation arising in the Board will be referred immediately to the Chairman for appropriate disposition.

(b) Employees of another agency of the Government who are detailed to the Board for a period of time which is anticipated to equal or exceed 1 year shall submit a signed statement to the Executive Secretary that they are conducting themselves in compliance with the standards, rules, or regulations of conduct in force in their own detailing agency. Since their own agency regulations cover similar subject matter, they will not be required to comply with this regulation, except as to the necessity for obtaining consent to certain outside activities including teaching, speaking, and writing for publication (see § 302.38(b)).

§ 302.5 Disciplinary and other remedial actions.

(a) A violation of any part of this regulation by a Board member, employee, or special Government employee may be cause for appropriate disciplinary action which may be in addition to any penalty prescribed by law.

(b) When, after consideration of the explanation of the employee or special Government employee provided by § 302.85, the Chairman decides that remedial action is required, he shall take immediate steps to end the conflict of interest or the appearance of conflict of interest. Remedial action may include one or more of the following, but is not limited to them:

(1) Changes in assigned duties;

(2) Divestment by the employee or special Government employee of his conflicting interest;

(3) Disciplinary action;

(4) Disqualification for a particular assignment.

§ 302.6 Effecting disciplinary and remedial actions.

Remedial action, whether disciplinary or otherwise, shall be effected in accordance with applicable laws and regulations.

§ 302.7 Release of information.

(a) The Board may from time to time publish or release statements of practice and policy, as well as those matters required to be published, or made available to the general public by 5 U.S.C. 552 and those proposed and final standards, rules, and regulations required to be published in the FEDERAL REGISTER by section 719 of Pub. L. 91-379.

(b) Proposals, working papers, staff papers, and similar writings which have not been so published or made available to the general public shall be considered as privileged internal Board matters, and no publication of them or comments on them shall be made to the general public, and no information relating to them shall be divulged to the general public by any Board member, employee, or special Government employee, without prior approval of the Chairman.

(c) The prohibition contained in this paragraph regarding premature release or discussion of internal Board matters is not intended in any way to prevent or hamper Board members, employees, or special Government employees from correspondence or discussion of Board matters and writings with others in the proper discharge of their duties. It is, however, designed to facilitate confidential discussions within the Board and to prevent disclosure of confidential or non-public information. It is in addition to statutory prohibitions and other provisions of this regulation (see §§ 302.32, 302.33, 302.38, 302.52, and 302.53) covering use of information obtained as a result of membership on or employment with the Board.

§ 302.8 Distribution of regulation.

(a) A copy of this regulation shall be furnished each Board member, employee, and special Government employee.

(b) Copies of pertinent laws and instructions relating to ethical and other conduct will be made available in the Office of the General Counsel of the Board, upon request by Board members, employees, and special Government employees.

Subpart B—Regulation Governing Ethical and Other Conduct and Responsibilities of Board Members

§ 302.11 General provisions.

(a) A Board member who is also an officer or employee of an agency or department in the legislative or executive branch of the U.S. Government or of any independent agency of the United States or of the District of Columbia is subject to the laws, regulations, and requirements affecting that office or employment and shall be subject to this regulation only to the extent that it establishes duties or responsibilities relating particularly to service with the Cost Accounting Standards Board.

(b) All other Board members are employees or special Government employees as defined in § 302.2. They are subject to the provisions of this regulation as employees or as special Government employees, except in those cases where a rule or requirement is stated herein as applicable specifically to Board members. (See §§ 302.5(a), 302.72(a), 302.75(a), and 302.82.)

Subpart C—Regulation Governing Ethical and Other Conduct and Responsibilities of Employees

§ 302.21 General policy on conduct.

The personal demeanor of employees of the Board is subject to the closest public and official scrutiny; and as representatives of the Board, employees are judged by their personal associates and activities as well as by their official actions and conduct. In all their dealings, employees of the Board shall so conduct themselves as to permit no reasonable basis for suspicion of unethical conduct or practices. The obligation to protect fully the interests of the Government as a whole and the Board as an agency of the Congress, demands the avoidance of circumstances which invite conflict between self-interest and the integrity of employment with the Board. Loyalty to the Board and its programs and purposes is a necessary attribute.

§ 302.22 Proscribed actions.

An employee shall avoid any action, whether or not specifically prohibited by this subpart, which might result in, or create the appearance of:

(a) Using public office for private gain;

(b) Giving improper preferential treatment to any person;

(c) Impeding Government efficiency or economy;

(d) Losing complete independence or impartiality;

(e) Making a Government decision outside official channels; or

(f) Affecting adversely the confidence of the public in the integrity of the Government or its operations.

§ 302.23 Gifts, entertainment, and favors.

Except as provided in §§ 302.24 and 302.27 of this subpart, an employee shall not solicit or accept, directly or indirectly, any gift, gratuity, favor, entertainment, loan, or any other thing of monetary value, from a person who:

(a) Has, or is seeking to obtain, contractual or other business or financial relations with the Federal Government;

(b) Conducts operations or activities that are subject to audit, investigation, decision, or regulation by the Board;

(c) Has interests that may be substanatially affected by the performance or nonperformance of the employee's official duty.

§ 302.24 Permissible gifts, entertainment, and favors.

Despite the limitations established by § 302.23 of this subpart, the following exceptions are made:

(a) A gift, gratuity, favor, entertainment, loan, or other similar favor of monetary value may be accepted by the employee when it or they stem from a family or personal relationship, such as those between the employee and his parents, children, or spouse, and when the circumstances make it clear that it is those relationships rather than the business of the persons concerned which are the motivating factors.

(b) Food and refreshments of nominal value may be accepted on infrequent occasions in the ordinary course of a luncheon or dinner meeting or other meeting or on an inspection tour where the employee may properly be in attendance.

(c) Loans from banks and other financial institutions may be accepted on customary terms to finance the proper and usual activities of employees, such as home mortgage loans.

(d) Unsolicited advertising or promotional material, such as pens, pencils, note pads, calendars, and other items of nominal value may be accepted.

§ 302.25 Gifts to superiors.

An employee shall not solicit a contribution from another employee for a gift to an official superior, make a donation as a gift to an official superior, or accept a gift presented as a contribution from an employee receiving less pay than himself (5 U.S.C. 7351).

§ 302.26 Gifts from foreign governments.

An employee shall not accept a gift, present, decoration, or other thing from a foreign government unless authorized by Congress as provided by the U.S. Constitution and in Pub. L. 89-673, 80 Stat. 952.

§ 302.27 Reimbursement of travel and living expenses.

Neither § 302.23 nor § 302.38 of this subpart precludes an employee from receipt of bona fide reimbursement, unless prohibited by law, for expenses of travel and such other necessary subsistence as is compatible with this subpart when not engaged on official business. However, this paragraph does not allow an employee to be reimbursed, or payment to be made on his behalf, for excessive personal living expenses, gifts, entertainment, or other personal benefits. When traveling on official business, no reimbursement may be accepted from private sources.

NOTE: Notwithstanding this paragraph, the requirements relating to the acceptance of contributions and awards, travel, subsistence and other expenses in section 4111(a), 5 U.S.C. and the regulations thereunder in Subpart G, Part 410, Book III, Supplement 990-1, Federal Personnel Manual, continue to apply.

§ 302.28 Indebtedness of employees.

An employee shall pay each just financial obligation in a proper and timely manner, especially one imposed by law such as Federal, State, or local taxes. For the purposes of this paragraph, a "just financial obligation" means one acknowledged by the employee or reduced to judgment by a court, and "in a proper and timely manner" means in a manner which the Board determines does not, in the circumstances, reflect adversely on the Board as his employer. In the event of a dispute between an employee and an alleged creditor, this paragraph does not require the Board to determine the validity of the disputed debt.

§ 302.29 Reports on indebtedness.

While the Board will not become a collection agency for private creditors of an employee, each complaint of nonpayment of a debt will be referred to the employee concerned and the employee will be requested to report in writing as to what he proposes to do about the debt.

§ 302.30 Gambling, betting, and lotteries.

An employee shall not participate, while on Government owned or leased property or while on duty for the Government, in any gambling activity including the operation of a gambling device, in conducting a lottery or pool, in a game for money or property, or in selling or purchasing a numbers slip or ticket.

§ 302.31 Use of Government property.

An employee shall not directly or indirectly use, or allow the use of, Government property of any kind, including property leased to the Government, for other than officially approved activities. An employee has a positive duty to protect and conserve Government property, including equipment, supplies, and other property entrusted or issued to him.

§ 302.32 Misuse of information.

For the purpose of furthering a private interest, an employee shall not, except as provided in section (b) of this subpart, directly or indirectly use, or allow the use of, official information obtained through or in connection with his Government employment which has not been made available to the general public.

§ 302.33 Prohibited financial interests.

An employee shall not:

(a) Have a direct or indirect financial interest that conflicts substantially or appears to conflict substantially with his Government duties and responsibilities.

(b) Engage in, directly or indirectly, a financial transaction as a result of, or primarily relying on, information obtained through his Government employment.

§ 302.34 Bribery, graft, and conflicts of interest.

An employee shall not engage in acts prohibited by Chapter 11 of Title 18, United States Code, relating to bribery, graft, and conflicts of interest as appropriate to the employee concerned. Three of the more important "conflict of interest" provisions are summarized as follows:

(a) An employee may not, except as provided by law for the proper discharge of his official duties, receive, agree to receive, ask, or seek any compensation for services by him or another in connection with any proceeding, request for a ruling, or other determination before any Government agency or officer in which the United States is a party or has a direct and substantial interest (18 U.S.C. 203).

(b) An employee may not, except in the discharge of his official duties, represent anyone else (with or without compensation) before a court or Government agency in a matter in which the United States is a party or has a direct or substantial interest (18 U.S.C. 205).

(c) An employee shall not receive any salary or anything of monetary value from a private source as compensation for his services to the Government (18 U.S.C. 209).

§ 302.35 Conflicts resulting from assignments.

An employee will not participate in any audit, investigation, survey, examination, ruling, decision or determination, contract, claim, controversy, or other matter before the Board in which he, his spouse, minor child, partner, organization in which he is serving as officer, director, trustee, partner or employee, or any person or organization with whom he is negotiating or has any arrangement concerning prospective employment, has a financial interest, with the following exceptions:

(a) The employee need not disqualify himself if his financial holdings are in shares of widely held diversified mutual funds or regulated investment companies in which he does not serve as director, officer, partner, or advisor. The indirect interest in business entities which the holder of shares in a widely diversified mutual fund or regulated investment company of stocks in business entities is hereby exempted from the provisions of 18 U.S.C. 208(a) in accordance with the provisions of 18 U.S.C. 208(b)(2) as being too remote or inconsequential to affect the integrity of the employee's services.

(b) If the employee first informs the Chairman through the Executive Secretary, in writing, of the nature and circumstances of the audit, investigation, survey, examination, ruling, decision or determination, contract, claim, controversy, or other matter in which he is participating and makes full disclosure of the financial interest and receives in advance a written determination made by the Chairman that the interest is not so substantial as to be deemed likely to affect the integrity of the employee's services, the employee need not consider himself disqualified (18 U.S.C. 208(b)).

§ 302.36 Disqualification procedure.

Where the employee, his spouse, minor child, partner, organization in which he is serving as officer, director, trustee, partner or employee, or any person with whom he is negotiating or has an arrangement concerning prospective employment, has a financial interest in any matter in which he is participating as part of his official duties, he will so inform the Chairman through the Executive Secretary, in writing, and he will thereupon be relieved of his duties and responsibilities in that particular matter unless the Executive Secretary, after consultation with and the approval of the Chairman finds that pursuant to § 302.35(b) of this subpart, the interest is too remote or too inconsequential to affect the integrity of the employee's services, in which case the Chairman will so notify the employee in writing. In cases of disqualification of the employee, the assignment of the employee will be changed, or the matter will be reassigned to another employee. A memorandum of disqualification will be made and forwarded by the Chairman to the employee with copies to the Executive Secretary and the Counselor for the Board.

§ 302.37 Nondisqualifying interests.

This subpart does not preclude an employee from having a financial interest or engaging in financial transactions to the same extent as a private citizen not employed by the Government so long as it is not prohibited by applicable law or regulations.

§ 302.38 Outside employment and other activity.

(a) An employee shall not engage in outside employment or other outside activity not compatible with the full and proper discharge of the duties and responsibilities of his Government employment. Incompatible activities include but are not limited to:

(1) Acceptance of a fee, compensation, gift, payment of expense, or any other thing of monetary value in circumstances in which acceptance may result in, or create the appearance of, a conflict of interest;

(2) Outside employment which tends to impair his mental or physical capacity to perform his Government duties and responsibilities in an acceptable manner.

(b) Employees may (subject to the provisions of paragraph (c)(3) of this section) engage in teaching, lecturing, and writing that is not prohibited by law or these regulations. An employee shall not, however, either for or without compensation, engage in teaching, lecturing, or writing, including teaching, lecturing, or writing for the purpose of the special preparation of a person or class of persons for an examination of the Civil Service Commission or Board of Examiners for the foreign service, that depends on information obtained as a result of his Government employment, except when that information has been made available to the general public or will be made available on request, or when the Chairman gives written authorization for the use of nonpublic information on the basis that such use is in the public interest.

(c) This paragraph does not preclude an employee from:

(1) Participation in the activities of national or State political parties not precluded by law;

(2) Participation in the affairs of or acceptance of an award for a meritorious public contribution or achievement given by a charitable, religious, professional, social, fraternal, nonprofit, educational and recreational, public service, or civic organization;

(3) Outside employment when permission has been granted in advance by the Executive Secretary or his designee, and the employee has been notified in writing of the approval. This permission will be granted in accordance with the following policies, procedures, and limitations:

(i) In considering requests for outside employment, the following criteria will be applied—the provisions of applicable law, the regulations and policies incorporated in this subpart including the possibility of conflicts of interest, the general attendance record of the employee, the nature of his official duties in relation to the nature of the duties which will comprise the outside employment; the financial need or other justification for such outside employment, and the hours of work required by the outside employment;

(ii) An employee will request permission to engage in outside employment by executing, in full, GAO Form 256 (Rev. 10/67) and forwarding it through his immediate supervisor to the Executive Secretary or his designee;

(iii) The Executive Secretary or his designee will, upon receipt of a fully executed GAO Form 256 (Rev. 10/67), evaluate the request in light of existing law and policies and regulations;

(iv) The Executive Secretary or his designee will officially approve or disapprove the request, and the employee will be notified. If the action taken on the request is not agreed to by the employee, the request and all recommendations will be submitted to the chairman for ultimate determination. The chairman will thereupon consider the entire record, make the final determination, and cause the employee to be notified;

(v) Grants of permission to engage in outside employment will normally expire 3 calendar years from the date of last issue, unless sooner revoked or modified. Permission to engage in outside employment which is about to expire will be considered for renewal upon receipt of a request on GAO Form 256 (Rev. 10/67). Procedures for renewal will be the same as those for original application and should be made, if continuity of permission is desired, from 30 to 60 days before the expiration of current permission;

(vi) Permission to engage in outside employment extends only to the specific employment described in the request considered. New requests must be made in writing in accordance with these procedures to cover any changes or modifications in outside employment;

(vii) An employee with permission to engage in outside employment will not hold himself out to the public as an attorney or accountant by such means as:

(*a*) Placing his name on an office door, (*b*) Having his name listed in the classified section of the telephone directory, or

(*c*) Using business stationery with his name on letterheads or envelopes.

(viii) Permission to engage in outside employment will not be granted for the purpose of representing clients in court or before Government agencies except in rare cases when permission may be granted for specific appearances;

(ix) An employee may be permitted to engage in income tax work and to sign income tax returns as a preparer, provided:

(*a*) The taxpayer has no Government contracts and has no business with the U.S. Government,

(*b*) The employee does not in any manner intercede with or appear for the taxpayer before the Internal Revenue Service, the courts, or other Government body.

(x) An employee may not use his employment with the Board as a means of soliciting or obtaining outside employment;

(xi) An employee may not engage in outside employment while he is on sick leave from his duties. Deviations from this policy may be permitted in rare instances when prior approval is obtained from the Executive Secretary;

(xii) Employees in grades equivalent to GS-13 and higher will not, normally, be given permission to engage in outside employment. Exceptions will be made for good and sufficient reasons, such as where a critical need exists for additional income by the employee or where the employment is found to be in the public interest in terms of opportunity for valuable experience beneficial both to the employee and to the Board. Each request for an exception under this paragraph shall be in sufficient detail to permit a judgment that it is merited. If an exception is made for employees in grades equivalent to GS-13 and higher, permission will be granted for 1-year intervals.

§ 302.39 Articles and speeches.

Employees who prepare, with or without compensation, articles for publication and speeches for delivery shall submit drafts thereof to the Executive Secretary or his designee prior to publication or delivery when:

(a) Any reference is made or to be made to the employee's employment by the Board.

(b) The subject of the article or speech concerns the work of the Board.

§ 302.40 File of articles and speeches.

The Board Library will maintain a permanent file of all published articles and speeches by employees of the Board. In order that this file be complete and current each employee who has had an article published or has made a speech shall send two copies thereof to the library.

§ 302.41 General conduct prejudicial to the Government.

An employee shall not engage in criminal, infamous, immoral, or notorious disgraceful conduct, or other conduct prejudicial to the Government, nor shall he conduct himself in such a manner as to give rise to a reasonable belief that he is engaging in criminal, infamous, immoral, or notorious disgraceful conduct.

§ 302.42 Miscellaneous statutory provisions.

Each employee will acquaint himself with each statute that relates to his ethical and other conduct as an employee of the Board with particular reference to the following:

(a) House Concurrent Resolution 175, 85th Congress, second session, 72 Stat. B12, the "Code of Ethics for Government Service."

(b) Chapter 11 of Title 18, United States Code, relating to bribery, graft, and conflicts of interest, as appropriate to the employees concerned.

(c) The prohibition against lobbying with appropriated funds (18 U.S.C. 1913).

(d) The prohibitions against disloyalty and striking (5 U.S.C. 7311, 18 U.S.C. 1918).

(e) The prohibition against the employment of a member of a Communist organization (50 U.S.C. 784).

(f) The prohibitions against (1) the disclosure of classified information (18

U.S.C. 798, 50 U.S.C. 783); and (2) the disclosure of confidential information (18 U.S.C. 1905).

(g) The provision relating to the habitual use of intoxicants to excess (5 U.S.C. 7352).

(h) The prohibition against the misuse of a Government vehicle (31 U.S.C. 638a(c)).

(i) The prohibition against the misuse of the franking privilege (18 U.S.C. 1719).

(j) The prohibition against interference with civil service examinations (18 U.S.C. 1917).

(k) The prohibition against fraud or false statement in a Government matter (18 U.S.C. 1001).

(l) The prohibition against mutilating or destroying a public record (18 U.S.C. 2071).

(m) The prohibition against counterfeiting and forging transportation requests (18 U.S.C. 508).

(n) The prohibitions against (1) embezzlement of Government money or property (18 U.S.C. 641); (2) failing to account for public money (18 U.S.C. 643); and (3) embezzlement of the money or property of another person in the possession of an employee by reason of his employment (18 U.S.C. 654).

(o) The prohibition against unauthorized use of documents relating to claims from or by the Government.

(p) The prohibition against proscribed political activities—in Subchapter III of Chapter 73 of Title 5, United States Code, and 18 U.S.C. 602, 603, 607, and 608.

(q) The prohibition against an employee acting as the agent of a foreign principal registered under the Foreign Agents Registration Act (18 U.S.C. 219).

Excerpts from the more important statutes of general applicability are quoted in Appendix A to Comptroller General's Order No. 1.21.

Subpart D—Regulation Governing Ethical and Other Conduct and Responsibilities of Special Government Employees

§ 302.51 Use of Government employment.

A special Government employee shall not use his Government employment for a purpose that is, or gives the appearance of being, motivated by the desire for private gain for himself or another person, particularly one with whom he has family, business, or financial ties.

§ 302.52 Use of inside information.

A special Government employee shall not use inside information obtained as a result of his Government employment for private gain for himself or another person either by direct action on his part or by counsel, recommendation, or suggestion to another person, particularly one with whom he has family, business, or financial ties. For the purposes of this paragraph, "inside information" means information obtained by reason of his Government employment which has not been made available to the general public.

§ 302.53 Teaching, lecturing, and writing.

A special Government employee may, without prior approval, teach, lecture, or write in a manner not otherwise inconsistent with §§ 302.32 and 302.38 of Subpart C of this regulation.

§ 302.54 Coercion.

A special Government employee shall not use his Government employment to coerce, or give the appearance of coercing, a person to provide financial benefit to himself or another person, particularly one with whom he has family, business, or financial ties.

§ 302.55 Gifts, entertainment, and favors.

Except as provided in § 302.24 of Subpart C of this regulation (as in the case of employees), a special Government employee, while so employed or in connection with his employment, shall not receive or solicit, either for himself or another person, particularly one with whom he has family, business, or financial ties, anything of value as a gift, gratuity, loan, entertainment, or favor from a person who:

(a) Has, or is seeking to obtain, contractual or other business or financial relations with the Board.

(b) Has an interest that may be substantially affected by the performance or nonperformance of his official duties.

§ 302.56 Miscellaneous statutory provisions.

Each special Government employee shall acquaint himself with each statute that relates to his ethical and other conduct as a special Government employee of the Board and the Government with particular reference to the statutes cited in § 302.42 of Subpart C of this regulation and the following:

(a) A special Government employee may not, otherwise than as provided by law for the proper discharge of his official duties, receive or agree to receive, or solicit any compensation for any services by himself or another, and may not, except in the proper discharge of his duties, represent or assist anyone, with or without compensation, before a department, agency, court, court-martial, officer, or any civil, military, or naval commission, in connection with a particular matter in which the United States is a party or has a direct or substantial interest: *Provided, however,* That these restrictions apply to a special Government employee only in relation to a particular matter involving a specific party or parties:

(1) In which he has at any time participated personally and substantially as a Government employee or special Government employee through decision, approval, disapproval, recommendation, the rendering of advice, investigation, or otherwise; or

(2) Which is pending in the department or agency of the Government in which he is serving, except that this provision (§ 302.56(a)(2) of this subpart) shall not apply when he has served in such department or agency no more than 60 days during the immediately preceding period of 365 days. He is bound by the restraint of this provision despite the fact that the matter is not one in which he has ever participated personally and substantially (18 U.S.C. 203, 205).

(b) A special Government employee shall not participate in his governmental capacity in any matter in which to his knowledge he, his spouse, minor child, partner, organization in which he is serving as officer, director, trustee, partner or employee, or any person or organization with whom he is negotiating or has any arrangement concerning prospective employment, has a financial interest (18 U.S.C. 208).

(c) After his Government employment has ended, a special Government employee is subject to the prohibition pertaining to a "former employee" in matters connected with his former duties (18 U.S.C. 202(a), 207).

(d) To the extent that the conflict of interest statutes apply to a special Government employee, they apply to his activities on all days during the period of his appointment to the Board, beginning with the date on which he takes an oath of office as a Government employee, whether he works on a full-time or intermittent basis. Similarly, the ethical standards prescribed in this subpart apply to the special Government employee during the full period of his appointment as an employee, and not merely on the days on which he performs services as an employee.

Subpart E—Prohibited Activities by Former Employees

§ 302.61 Prohibited activities.

A former employee shall not:

(a) At any time after his Government employment has ended, knowingly represent anyone other than the United States in connection with a matter in which the United States is a party or has an interest and in which he participated personally and substantially for the Government (18 U.S.C. 207(a)).

(b) For 1 year after his Government employment has ended, appear personally before any court or Government agency as agent or attorney for anyone other than the Government in connection with a matter in which the Government is a party or has a substantial interest and which was under his official responsibility as an employee of the Government at any time during the last year of his Government employment (18 U.S.C. 202(b) and 207(b)).

Subpart F—Regulation Governing Statements of Employment and Financial Interests

§ 302.71 Form and content of statements.

(a) The statements of employment and financial interests required to be submitted by this subpart shall contain, as a minimum, the information required by GAO Form 310 (Rev. 9/67) and GAO Form 311 (Rev. 9/67), respectively.

(b) The submission of a statement of employment and financial interests is not intended to relieve the employee from complying with other applicable provisions of law or this regulation. In particular, the employee is not thereby permitted to participate in a matter where such participation is prohibited by 18 U.S.C. 208.

§ 302.72 Requirement to submit statements.

Except as otherwise provided in this regulation, statements of employment and financial interests (GAO Form 310, Rev. 9/67) will be required from the following:

(a) Board members and the Executive Secretary and any staff assistant to a Board member. Any Board member filing equivalent statements of employment and financial interests in connection with his employment at another Federal agency shall not be required to submit this information in connection with employment at the Board.

(b) Employees in positions equivalent to grades GS-14 or above under the Federal Employees Classification Act.

(c) Special Government employees, subject to the provisions of §§ 302.87-302.90, inclusive, of this subpart.

§ 302.73 Employees not required to submit statements.

Employees in positions equivalent to grades GS-13 and below under the Federal Employees Classification Act are excluded from the reporting requirement of § 302.72 of this subpart. The likelihood of their involvement in a conflicts-of-interest situation is remote or the degree of supervision over them and the review of their work is such that the integrity of the Government is protected. This paragraph does not in any way modify or limit any employee's responsibilities under §§ 302.33-302.36, inclusive, of Subpart C of this regulation.

§ 302.74 Employee's complaint on filing requirement.

An employee who feels that his position has been improperly included by this subpart as one requiring the submission of a statement of employment and financial interests may obtain a review of that requirement by filing a grievance with the Chairman.

§ 302.75 Where to submit statements.

(a) The Chairman will file a statement of employment and financial interests (GAO Form 310) with the Director, Office of Personnel Management, General Accounting Office, who will retain it. The other Board members, the Executive Secretary and staff assistants will file a statement of employment and financial interests (GAO Form 310) with the Chairman.

(b) Employees required to submit a statement of employment and financial interests will submit their statements (GAO Form 310) to the Executive Secretary.

§ 302.76 When to submit statements.

Each employee required to submit a statement of employment and financial interests shall submit that statement to the appropriate officer designated in § 302.75 of this subpart.

(a) Ninety days after the effective date of this regulation, if employed on or before that effective date (unless the employee has already submitted a statement as required by this regulation and that statement continues to be accurate).

(b) Thirty days after his entrance on duty in or after his promotion to a position subject to this subpart.

§ 302.77 Supplementary statements.

Changes in, or additions to, the information contained in an employee's statement of employment and financial interests shall be reported in a supplementary statement as of June 30 of each year in which the changes occur. If no changes or additions occur, a negative report is required. Notwithstanding the filing of the annual report required by this paragraph, each employee shall at all times avoid acquiring a financial interest that could result in taking an action that would result in a violation of the conflicts-of-interest provisions of section 208 of Title 18, United States Code, or Subparts C and D of this regulation.

§ 302.78 Interests of employees' relatives.

The interest of a spouse, minor child, or other member of an employee's immediate household is considered to be an interest of the employee. For the purpose of this paragraph, "member of an employee's immediate household" means those relatives by blood who are residents of the employee's household.

§ 302.79 Information not known by employees.

If any information required to be included on a statement of employment and financial interests or supplementary statement, including holdings placed in trust, is not known to the employee but is known to another person, the employee shall request that other person to submit information in his behalf.

§ 302.80 Information not required.

(a) This regulation does not require an employee to submit on a statement of employment and financial interests or supplementary statement any information relating to the employee's connection with, or interest in, a professional society or a charitable, religious, social, fraternal, recreational, public service, civic, or political organization or a similar organization not conducted as a business enterprise. For the purpose of this paragraph, education and other institutions doing research and development or related work involving grants of money from or contracts with the Government are deemed "business enterprises" and are required to be included in an employee's statement of employment and financial interests.

(b) An employee need not report on his statement of employment and financial interests shares of widely held, diversified mutual funds or regulated investment companies in which he does not serve as director, officer, partner, or advisor. The indirect interest in business entities which the holder of shares in a widely diversified mutual fund or regulated investment company derives from ownership by the fund of investment company of stocks in business entities is considered too remote or inconsequential to affect the integrity of the employee's services.

§ 302.81 Confidentiality of statements.

Statements of employment and financial interests and supplementary statements shall be retained in a confidential file secured in an appropriate manner by the Chairman or the Executive Secretary. No persons other than the Chairman or the Executive Secretary, as to employees or special Government employees under his direction, or the Counselor for the Board shall have access to such statements and then only to carry out the purposes of this regulation. No disclosure of information shall be made from such statements except as specifically authorized by the Chairman for good cause shown.

§ 302.82 Review of statements by the Chairman.

The Chairman and the Counselor for the Board, if requested to do so by the Chairman, will review each statement of employment and financial interests and each supplementary statement submitted directly to the Chairman by reason of § 302.75(a) of this subpart, as well as all relevant information from other sources incident thereto to determine whether there are any conflicts of interest or apparent conflicts of interest. Where no conflicts of interest or apparent conflicts of interest are found, the cases will be considered resolved unless other pertinent information becomes available. If questions of conflicts of interest or apparent conflicts of interest arise, pertinent procedures established for employees and special Government employees elsewhere in this regulation will be followed.

§ 302.83 Review of statements by the Executive Secretary.

The Executive Secretary, for other employees or special Government employees, together with the Counselor for the Board, will review each statement of employment and financial interests, each supplementary statement, and all relevant information from other sources, if any, to determine whether there are any conflicts of interest or apparent conflicts of interest on the part of the employee or special Government employee submitting the statement. If it is pertinent to a conflict-of-interest decision, the Executive Secretary may request the employee or special Government employee to supplement the information on GAO Form 310 or GAO Form 311 by stating the number or amount of shares, stock options, bonds, and other securities owned by him, his spouse, minor child, or other members of his immediate household.

§ 302.84 Findings of no conflict of interest.

If the Executive Secretary believes that there are no conflicts of interest or apparent conflicts of interest in individual cases, the matter will be considered resolved unless other information on the case becomes available or circumstances change.

§ 302.85 Findings of conflict of interest.

With respect to statements of employment and financial interests reviewed by the Executive Secretary under § 302.83 of this subpart, when the Executive Secretary or the Counselor for the Board believes that the statement or information from other sources discloses a conflict of interest or an apparent conflict of interest, the employee or special Government employee concerned will be asked to explain the conflict or appearance of conflict. If his explanation is satisfactory, the case will be considered closed unless further information or changed circumstances reactivate it. If there is believed to be a conflict or apparent conflict of interest on the part of the employee or special Government employee, a report will be made of the case to the Chairman for final disposition. This report will contain the views of the Executive Secretary and those of the Counselor for the Board, will point out specifically the areas of conflict or apparent conflict and the reasons why it is felt that a conflict or apparent conflict exists or does not exist, and will be signed by both these officials. The report will also contain a summary of the employee's explanation signed by him. The Chairman will then consider the matter, afford the employee or special Government employee concerned an opportunity to explain the conflict or apparent conflict, make a final decision, and take appropriate action in accordance with §§ 302.5(b) and 302.6 of Subpart A.

§ 302.86 Effect of employees' statements on other requirements.

The statement of employment and financial interests and supplementary statements required of employees are in addition to, and not in substitution for, or in derogation of, any similar requirement imposed by law, order, or regulation. The submission of a statement of employment and financial interests or supplementary statement by an employee does not permit him or any other person to participate in a matter in which his or the other person's participation is prohibited by law, order, or regulation.

§ 302.87 Specific provisions for special Government employees.

Except as provided in § 302.88 of this subpart, each special Government employee, by the use of GAO Form 211 (Rev. 9/67), shall submit a statement of employment and financial interests which reports:

(a) All other employment; and

(b) The financial interests of the special Government employee as indicated on GAO Form 311. A special Government employee need not report financial interests in widely held, diversified mutual funds or regulated investment companies in which he does not serve as director, officer, partner, or advisor.

§ 302.88 Waiver of statements from certain special Government employees.

(a) The provisions of § 302.87 of this subpart are waived for special Government employees who are employed for the purpose of rendering advice, counsel, or expert services on recruiting and staff development including CPA review courses, because such employment is of a nature and at such a level of responsibility that any financial interests that they may have would be too remote to affect the integrity of their services to the Board and the submission of statements would be unnecessary.

(b) In addition, the Chairman may waive the requirement of § 302.87 of this subpart for the submission of a statement of employment and financial interests in the case of a special Government employee when he finds that the duties performed by that special Government employee are of a nature and at such level of responsibility that the submission of the statement by the special Government employee is not necessary to protect the integrity of the Board.

§ 302.89 Time for submission of statements by special Government employees.

A statement of employment and financial interests required to be submitted under § 302.87 of this subpart shall be submitted not later than the time of employment of the special Government employee. Each special Government employee shall keep his statement current throughout his employment with the Board by submission of supplementary statements contained in his statement of employment and financial interests every 90 days after his appointment until he is no longer subject to § 302.87 of this subpart. Upon reappointment immediately following separation, the special Government employee shall file a new statement or certify that the latest statement on file is currently correct, whichever is proper.

§ 302.90 Circumstances requiring statements from special Government employees.

In all cases where the employment of a special Government employee to work on a specific audit, accounting, legal, or other problem is contemplated, or where a special Government employee already employed to render advice, counsel, or expert services on recruitment and staff development is to be assigned work on a specific audit, legal, or other problem, procedures outlined in §§ 302.83, 302.87, and 302.89 will be followed.

PART 303—RELEASE OF INFORMATION

Sec.

303.1 Purpose.
303.2 Records covered.
303.3 Exempted records.
303.4 Time and place where records may be inspected or copied.
303.5 Fees for copying.
303.6 Procedure for requesting records.
303.7 Production of board records.
303.8 Use of records.
303.9 Refusal to make record available.

AUTHORITY: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168 and 81 Stat. 54; 5 U.S.C. 552.

SOURCE: 36 FR 23923, Dec. 16, 1971, unless otherwise noted.

§ 303.1 Purpose.

This regulation describes the manner in which records of the Cost Accounting Standards Board shall be available for public inspection and copying.

§ 303.2 Records covered.

(a) As used herein, Board "records" include all interpretations, opinions, orders, manuals, papers, files, letters, memoranda, studies, reports, information, or other documentary materials in being other than documentary materials which are in the possession of the Board but which are records of another Government agency. Not included within Board "records" are objects, equipment, and other nondocumentary materials.

§ 303.3 Exempted records.

As used herein, "exempted records" include those Board records which, pursuant to 5 U.S.C. 552(b) or other applicable law or regulation, are not required to be made available generally for inspection or copying. Notwithstanding the fact that the Board is not required to do so, an exempted record may be made available when the Board in its discretion determines that such action is appropriate.

§ 303.4 Time and place where records may be inspected or copied.

Records may be inspected and copied at the Board's offices, General Accounting Office Building, 441 G Street, NW., Washington, D.C. during the Board's normal business hours, 8:30 a.m. to 5 p.m., local time, Monday through Friday, excluding holidays observed by the Federal Government in Washington, D.C.

§ 303.5 Fees for copying.

(a) The fee for searching for and duplicating Board records shall be $5.00 for each full hour of time required. No charge will be made for fractions of an hour.

(b) Any inquiry that appears to involve a total of more than 10 hours of search and duplication time will not be regarded as a request for information under this Part 303 unless this part is specifically cited or the inquirer specifically agrees to accept costs necessary to cover the estimated number of hours involved.

(c) Notwithstanding the foregoing, no charge or a reduced charge will be made whenever the Executive Secretary of the Cost Accounting Standards Board determines that a waiver or reduction of the fee is in the public interest because furnishing the information can be considered as primarily benefiting the general public.

[40 FR 18541, Apr. 29, 1975]

§ 303.6 Procedure for requesting records.

(a) A request to inspect or copy, or have copied, the Board's records may be made in person, by telephone, or in writing.

(b) Requests for records shall be specific and must identify the precise records or materials which are desired by name, date, number, or other identifying data sufficient to allow the Board's staff to locate, retrieve, and prepare the record for inspection or copying and to delete exempted matter where appropriate. Blanket or generalized requests need not be honored, and may be returned to the person making the request.

§ 303.7 Production of board records.

Every effort will be made to respond to requests with reasonable dispatch. Requests for the same record will be filled on a first-come, first-served basis, but use of a document by the Board or its staff will be given precedence over any request pursuant to this § 303.7.

§ 303.8 Use of records.

(a) If a person requesting a record cannot view it at the Board's offices during normal business hours, he may ask to have the record copied and mailed to him for which he will be charged the appropriate fee.

(b) Any record which is available for inspection at the Board's offices may be copied.

(c) Under no circumstances may records be removed from the Board's offices.

§ 303.9 Refusal to make record available.

(a) Where the material requested is not in being, is not a record, is an exempted record, or is otherwise unavailable, the request will be denied. The person making the request will be informed within 10 working days after receipt of the request for the material of the denial and the reason therefor.

(b) Not more than 20 days after a request for a record is denied pursuant to paragraph (a) of this section, the person making the request may appeal the denial to the Chairman, Cost Accounting Standards Board, who will make determinations on such appeals. The appeal shall be by letter, and shall identify the material requested and denied in the same manner as it was identified in the initial request; shall indicate the dates of the request and denial; and shall indicate the expressed basis for the denial. In addition, the letter of appeal shall state briefly and succinctly the reasons why the record should be made available.

(c) The Chairman may consult with others in making his determination, and shall by letter inform the requester, within 20 business days after receipt of the appeal, whether the requested material will be made available in whole or in part. If the request is denied in whole or in part, the basis for denial will be stated.

[40 FR 18541, Apr. 29, 1975]

PART 304—DELEGATIONS OF AUTHORITY

Sec.
304.1 Purpose.
304.2 Contracting authority.
304.3 Waivers and exemptions.
304.4 Fees for copying records.

Authority: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

§ 304.1 Purpose.

This part publishes all delegations of authority by the Board, except delegations dealing with internal administrative matters which do not affect the public.

[36 FR 23924, Dec. 16, 1971]

§ 304.2 Contracting authority.

(a) The Cost Accounting Standards Board hereby delegates to the Executive Secretary of the Board authority to enter into, administer, and settle contracts in furtherance of the Board's duties and responsibilities and designates the Executive Secretary as Contracting Officer of the Cost Accounting Standards Board.

(b) This authority, including authority to designate successor contracting officers, may be redelegated.

(c) This delegation is effective the date hereof and until revoked.

[36 FR 23924, Dec. 16, 1971]

§ 304.3 Waivers and exemptions.

(a) The Cost Accounting Standards Board hereby delegates to the Executive Secretary of the Board, acting in consultation with the Chairman of the Board, authority to exercise the Board's authority under § 331.3(c) of the Board's Contract Coverage (4 CFR 331.3(c)) of its rules and regulations, providing the Executive Secretary concludes that a request for an exemption or waiver submitted pursuant to that § 331.3(c) must be acted on before he can obtain the required number of opinions of the members of the Cost Accounting Standards Board on that request.

(b) This authority may not be redelegated.

(c) This delegation is effective February 26, 1973, and until revoked.

[38 FR 5621, Mar. 2, 1973]

§ 304.4 Fees for copying records.

(a) The Cost Accounting Standards Board hereby delegates to the Executive Secretary of the Board authority to exercise the Board's authority under § 303.5(a), release of information (4 CFR 303.5(a)), of its rules and regulations.

(b) This authority may be redelegated.

(c) This delegation is effective July 25, 1973 and until revoked.

[38 FR 19831, July 24, 1973]

PART 305—COST ACCOUNTING STANDARDS BOARD BYLAWS

Sec.
305.1 Purpose.
305.2 Membership.
305.3 Quorum.
305.4 Board action.
305.5 Meetings.
305.6 Executive sessions.
305.7 Minutes.
305.8 Amendments to these bylaws.

Authority: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

Source: 36 FR 23924, Dec. 16, 1971, unless otherwise noted.

§ 305.1 Purpose.

This part publishes the bylaws adopted by the Board to govern Board membership, meetings, and formal actions by Board vote.

§ 305.2 Membership.

The Board is composed of the Comptroller General of the United States and the four members appointed by him. In the event of the absence or incapacity of the Comptroller General or during a vacancy in the office, the official of the General Accounting Office acting as Comptroller General shall serve as Chairman of the Board. In the event of the absence of any of the other four Board members, a representative of that member may attend the Board meeting, but he shall have no vote, and his attendance shall not be counted to establish a quorum.

§ 305.3 Quorum.

Three Board members shall constitute a quorum of the Board.

§ 305.4 Board action.

Board action shall be by majority vote of the members present and voting, except that any vote to publish a proposed standard, rule, or regulation in the FEDERAL REGISTER for comment or any vote to promulgate a standard, rule, or regulation shall require at least three affirmative votes of the five Board members. The Chairman may vote on all matters presented for a vote, not merely to resolve tie votes. The results of final votes shall be reported in the minutes of the meeting, and the vote of a Board member may be recorded at his request.

§ 305.5 Meetings.

The Board shall meet at the call of the Chairman. Agenda for Board meetings shall be proposed by the Chairman, but any Board member may request any item to be placed on the agenda.

§ 305.6 Executive sessions.

Any Board member may request that the Board meet in executive session, and the Chairman shall thereupon order such a session.

§ 305.7 Minutes.

The Executive Secretary of the Board shall be responsible for keeping accurate minutes of Board meetings and for maintaining Board files.

§ 305.8 Amendments to these bylaws.

These bylaws may be supplemented or amended by the Board, but only after notice of the proposal to supplement or amend has been given in the call to the meeting. Any change in § 305.2, *Membership*, of this part must be in accord with the provisions of section 719 of Pub. L. 91-379, 50 U.S.C. App. 2168.

SUBCHAPTER B—[RESERVED]

SUBCHAPTER C—PROCUREMENT PRACTICES

PART 331—CONTRACT COVERAGE

Sec.
331.10 Purpose and scope.
331.20 Definitions.
331.30 Applicability, exemption, and waiver.
331.40 [Reserved]
331.50 Contract clause.
331.51 Findings.
331.60 Disclosure requirements.
331.70 Interpretation.
331.71 Materiality.
331.72 Relationship to Part 332.
331.80 Effective date.
PREAMBLES A—M

AUTHORITY: Sec. 103, 84 Stat. 796 (50 U.S.C. App. 2168).

SOURCE: 45 FR 62011, Sept. 18, 1980 unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in non-technical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (37 FR 4139, February 29, 1972) is set forth in preamble A of the supplement. The preambles to amendments affecting the original publication of this part are set forth in preambles B and C of the supplement.

The preamble to a complete revision and republication of this part (38 FR 30725, November 7, 1973) is set forth in preamble D of the supplement. For amendments affecting the complete revision and republication, see preambles E through L of the supplement.

Preamble M sets forth a complete revision and republication of this part (see 45 FR 62011, Sept. 18, 1980).

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 331.10 Purpose and scope.

The regulations contained in this part are promulgated to implement the standards and the rules and regulations established by the Cost Accounting Standards Board pursuant to 50 U.S.C. App. 2168 (Pub. L. 91-379, August 15, 1970). The requirements set forth herein shall be binding upon all relevant Federal agencies and upon defense contractors and subcontractors.

§ 331.20 Definitions.

(a) A "relevant Federal agency" is any Federal agency making a national defense procurement and any agency whose responsibilities include review, approval, or other action affecting such a procurement.

(b) A "defense contractor" is any person who enters into a contract with the United States for the production of material or the performance of services for the national defense.

(c) A "defense subcontractor" is any person other than the United States who contracts, at any tier, to perform any part of a defense contractor's contract.

(d) "National defense" is any program for military and atomic energy production or construction, military assistance to any foreign nations, stockpiling, space, and directly related activity.

(e) An "established catalog or market price of commercial items sold in substantial quantities to the general public" is as defined in the Defense Acquisition Regulation (32 CFR 3.807-1(b)), in effect at the date of the contract.

(f) A "negotiated subcontract" is any subcontract except a firm fixed-price subcontract made by a contractor or subcontractor after receiving offers from at least two persons not associated with each other or with such contractor or subcontractor, providing: (1) The solicitation to all competitors is identical, (2) price is the only consideration in selecting the subcontractor from among the competitors solicited, and (3) the lowest offer received in compliance with the solicitation from among those solicited is accepted.

(g) A "Disclosure Statement" is the Disclosure Statement required by Cost Accounting Standards Board regulation (Part 351 of this chapter).

(h) A "covered contract" is any negotiated national defense prime contract or subcontract which pursuant to requirements of the Cost Accounting Standards Board is required to include a Cost Accounting Standards clause (see 4 CFR Part 331 and this chapter).

(i) A "business unit" is any segment of an organization, or an entire business organization which is not divided into segments.

(j) A "segment" is one of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(k) A "cost accounting practice" is any disclosed or established accounting method or technique which is used for measurement of cost, assignment of cost to cost accounting periods, or allocation of cost to cost objectives.

(1) Measurement of cost encompasses accounting methods and techniques used in defining the components of cost, determining the basis for cost measurement, and establishing criteria for use of alternative cost measurement techniques. The determination of the amount paid or a change in the amount paid for a unit of goods and services is not a cost accounting practice. Examples of cost accounting practices which involve measurement of costs are:

(i) The use of either historical cost, market value, or present value;

(ii) The use of standard cost or actual cost; or

(iii) The designation of those items of cost which must be included or excluded from tangible capital assets or pension cost.

(2) Assignment of cost to cost accounting periods refers to a method or technique used in determining the amount of cost to be assigned to individual cost accounting periods. Examples of cost accounting practices which involve the assignment of cost to cost accounting periods are requirements for the use of specified accrual basis accounting or cash basis accounting for a cost element.

(3) Allocation of cost to cost objectives includes both direct and indirect allocation of cost. Examples of cost accounting practices involving allocation of cost to cost objectives are the accounting methods or techniques used to accumulate cost, to determine whether a cost is to be directly or indirectly allocated, to determine the composition of cost pools, and to determine the selection and composition of the appropriate allocation base.

(l) A "change to a cost accounting practice" is any alteration in a cost accounting practice, as defined in paragraph (k) of this section, whether or not such practices are covered by a Disclosure Statement, except that:

(1) The initial adoption of a cost accounting practice for the first time a cost is incurred, or a function is created, is not a change in cost accounting practice. The partial or total elimination of a cost or the cost of a function is not a change in cost accounting practice. As used here, function is an activity or group of activities that is identifiable in scope and has a purpose or end to be accomplished.

(2) The revision of a cost accounting practice for a cost which previously had been immaterial is not a change in cost accounting practice.

(m) *Illustrations of changes.* (1) In all of the following cases where a "change to a cost accounting practice" has taken place, modifications to the affected contracts would be considered in accordance with this Part 331, Contract Coverage, and Part 332, Modified Contract Coverage, as amended. In accordance with § 331.71, price adjustments, with appropriate application of offsets, would be required only if the net cost impact of the change were material.

(2) The following are illustrations of changes which meet the proposed definition of "change to a cost accounting practice" because:

(i) The method or technique used for measuring costs has been changed.

Description of changes	Accounting treatment
1. Contractor changes his actuarial cost method for computing pension costs.	1. (a) Before change: The contractor computed pension costs using the aggregate cost methods. (b) After change: The contractor computes pension cost using the unit credit method.
2. Contractor uses standard costs to account for his direct labor. Labor cost at standard was computed by multiplying labor-time standard by actual labor rates. The contractor changes the computation by multiplying labor-time standard by labor-rate standard.	(a) Before change: Contractor's direct labor cost was measured with only one component set at standard. (b) After change: Contractor's direct labor cost is measured with both the time and rate components set at standard.

(ii) The method or technique used for assignment of cost-to-cost accounting periods has been changed.

Description of change	Accounting treatment
1. Contractor changes his established criteria for capitalizing certain classes of tangible capital assests whose acquisition costs totaled $1 million per cost accounting period.	1. (a) Before change: Items having acquisition costs of between $200 and $400 per unit were capitalized and depreciated over a number of cost accounting periods. (b) After change: The contractor charges the value of assessts costing between $200 and $400 per unit to an indirect expense pool which is allocated to the cost objectives of the cost accounting period in which the cost was incurred.
2. Contractor changes his method for computing depreciation for a class of assests.	2. (a) Before change: The contractor assigned depreciation costs to costs accounting periods using an accelerated method. (b) After change: The contractor assigns depreciation costs to cost accounting periods using the straight line method.
3. Contractor changes his general method of determinating asset lives for classes of assets acquired prior to the effective date of CAS 409.	3. (a) Before change: The contractor identified the cost accounting periods to which the costs of tangible capital assets would be assigned using guideline class lives provided in IRS Rev. Pro. 72-10. (b) After change: The contractor changes the method by which he identifies the cost accounting periods to which the costs of tangible capital assets will be assigned. He now uses the expected actual lives based on past usage.

(iii) The method or technique used for allocating costs has been changed.

Description of changes	Accounting treatment
1. Contractor changes his method of allocating G&A expenses under the requirements of Cost Accounting Standard 410.	1. (a) Before change: The contractor operating under Cost Accounting Standard 410 has been allocating his general and administrative expense pool to final cost objectives on a total cost input base in compliance with the Standard. The contractor's business changes substantially such that there are significant new projects which have only insignficant quantities of material. (b) After change: After the addition of the new work, an evaluation of the changed circumstances reveals that the continued use of a total cost input base would result in a significant distortion in the allocation of the G&A expense pool in relation to the benefits received. To remain in compliance with Standard 410, the contractor alters his G&A allocation base from a total cost input base to a value added base.
2. The contractor changes the accounting for hardware common to all projects.	2. (a) Before change: The contractor allocated the cost of purchased or requisitioned hardware directly to projects. (b) After change: The contractor charges the cost of purchased or requisitioned hardware to an indirect expense pool which is allocated to projects using an appropriate allocation base.

Description of changes	Accounting treatment
3. The contractor merges operating segments A and B which use different cost accounting practices in accounting for manufacturing overhead costs.	3. (a) Before change: In segment A, the costs of the manufacturing overhead pool have been allocated to final cost objectives using a direct labor hours base; in segment B, the costs of the manufacturing overhead pool have been allocated to final cost objectives using a direct labor dollars base. (b) After change: As a result of the merger of operations, the combined segment decides to allocate the cost of the manufacturing overhead pool to all final cost objectives, using a direct labor dollars base. Thus, for those final cost objectives referred to in segment A, the cost of the manufacturing overhead pool will be allocated to the final cost objectives of segment A using a direct labor dollars base instead of a direct labor hours base.

(3) The following are illustrations of changes which do not meet the definition of "change to a cost accounting practice" and accordingly do not require price adjustments under the CAS contract clauses set forth in §§ 331.50 and 332.50.

Description of changes	Accounting treatment
1. Changes in the interest rate levels in the national economy have invalidated the prior actuarial assumption with respect to anticipated investment earnings. The pension plan administrators adopted an increased (decreased) interest rate actuarial assumption. The company allocated the resulting pension costs to all final cost objectives.	1. Adopting the increase (decrease) in the interest rate actuarial assumption is not a change in cost accounting practice.
2. The basic benefit amount for a company's pension plan is increased from $8 to $10 per year of credited service. The change increases the dollar amount of pension cost allocated to all final cost objectives.	2. The increase is the amount of the benefits is not a change in cost accounting practice.
3. A contractor who has never paid pensions establishes for the first time a pension plan. Pension costs for the first year amounted to $3.5 million.	3. The initial adoption of an accounting practice for the first time incurrence of a cost is not a change in cost accounting practice.
4. A contractor maintained a Deferred Incentive Compensation Plan. After several years' experience, the plan was determined not to be attaining its objective, so it was terminated, and no future entitlements were paid.	4. There was a termination of the Deferred Incentive Compensation Plan. Elimination of a cost is not a change in cost accounting practice.
5. A contractor eliminates a segment that was operated for the purpose of doing research for development of products related to nuclear energy.	5. The projects and expenses related to nuclear energy projects have been terminated. No transfer of these projects and no further work in this area is planned. This is an elimination of cost and not a change in cost accounting practice.
6. For a particular class of assets for which technological changes have rarely affected asset lives, a contractor starts with a five year average of historical lives to estimate future lives. He then considers technological changes and likely use. For the past several years the process resulted in an estimated future life of ten years for this class of assets. This year a technological change leads to a prediction of a useful life of seven years for the assets acquired this year for the class of assets.	6. The change in estimate (not in method) is not a change in cost accounting practice. The contractor has not changed the method or technique used to determine the estimate. The methodology applied has indicated a change in the estimated life, and this is not a change in cost accounting practice.
7. The marketing department of a segment has reported directly to the general manager of the segment. The costs of the marketing department have been combined as part of the segment's G&A expense pool. The company reorganizes and requires the marketing department to report directly to a vice president at corporate headquarters.	7. After the organizational change in the company's reporting structure, the parties agree that the appropriate recognition of the beneficial or causal relationship between the costs of the marketing department and the segment is to continue to combine these costs as part of the segment's G&A expense pool. Thus, the organizational change has not resulted in a change in cost accounting practice.

(n) A "small business concern" is any concern, firm, person, corporation, partnership, cooperative or other business enterprise which pursuant to 15 U.S.C. 637(b)(6) and the rules and regulations of the Small Business Administration set forth in Part 121 of Title 13 of the Code of Federal Regulations, is determined to be a small business concern for the purpose of Government procurement.

§ 331.30 Applicability, exemption, and waiver.

(a) The head of each relevant Federal agency shall cause or require a clause set forth in § 331.50 captioned Cost Accounting Standard to be inserted in all negotiated defense contracts in excess of $100,000, except as provided in paragraph (b) of this section, other than contracts entered into by the agency where the price is based on: (1) Established catalog or market prices of commerical items sold in substantial quantities to the general public, or (2) prices set by law or regulation.

(b) The requirements of paragraph (a) of this section shall not be applicable to:

(1) Any contract or subcontract awarded to a small business concern.

(2) Any contract or subcontract awarded for performance in a business unit which is eligible to use the provisions of Part 332 of the Board's regulations and which elects to use that part.

(3) Any contract or subcontract awarded to an educational institution whose cost principles are subject to Federal Management Circular 73-8 except contracts that are to be performed by a federally funded research and development center (FFRDC) operated by such an institution. A FFRDC is a laboratory or similar operation which is designated as such by the National Science Foundation. If a contract or any part of a contract awarded to an exempt educational institution is to be performed by a FFRDC, the contract shall contain the clause set forth in § 331.50 or § 332.50, as appropriate, and the requirements of that clause shall be applicable to that part of the contract effort, and the costs thereof, which are performed by the FFRDC. Costs incurred by the institution which may be allocated to the FFRDC are specifically exempted by this provision as is the requirement to prepare part VIII of the disclosure statement (CASB-DS-1 or CASB-DS-2).

(4) Any contract awarded to a labor surplus area concern pursuant to procedures providing for a partial set-aside for such concern as set out in DAR 1-804, 32 CFR 1-804, and FPR 1-1.804, 41 CFR 1-1.804.

(5) Any contract or subcontract awarded to a foreign government or an agency or instrumentality of such government or, insofar as the requirements of Cost Accounting Standards 403 (4 CFR Part 403) or any subsequent standards are concerned, any contract or subcontract awarded to a foreign concern.

NOTE: This exemption does not relieve foreign concerns of any obligation to comply with the Cost Accounting Standards set forth in 4 CFR Parts 401 and 402 and to submit a Disclosure Statement.

(6) Any subcontract to be performed outside the United States either by an agency of a foreign government or by a foreign concern in connection with the class of hydrofoil guided missile ship know as the "NATO PHM Ship."

(7) Any contract or subcontract of $500,000 or less, unless the business unit to whom it is awarded (i) is performing one or more covered contracts and (ii) has not received notification of final acceptance of all items of work to be delivered under all such contracts. For the purposes of this paragraph (b)(7) an order issued by one segment to another segment shall be treated as a subcontract.

(8) Any contract or subcontract awarded to a United Kingdom contractor for performance substantially in the United Kingdom: *Provided,* That the contractor has filed with the U.K. Ministry of Defence, for retention by the Ministry, a completed Disclosure Statement (Form CASB-DS-1) which shall adequately describe its cost accounting practices. Whenever that contractor is already required to follow U.K. Government Accounting Conventions, the disclosed practices shall be in accord with the requirements of those Conventions. Such contract or subcontract shall also contain the following provision:

CONSISTENCY IN COST ACCOUNTING PRACTICES

The contractor agrees that it will consistently follow the cost accounting practices disclosed on Form CASB-DS-1 in estimating, accumulating and reporting costs under this contract. In the event the contractor fails to follow such practices, it agrees that the contract price shall be adjusted, together with payment of interest, if such failure results in increased costs paid by the U.S. Government. Interest shall be determined in accordance with the rules and regulations of the Cost Accounting Standards Board. The contractor agrees that the Disclosure Statement filed with the U.K. Ministry of Defence shall be available for inspection and use by representatives of the contracting agency, the Cost Accounting Standards Board, and the Comptroller General of the United States.

(9) Any firm fixed price contract or subcontract awarded without submission of any cost data: *Provided*, That the failure to submit such data is not attributable to a waiver of the requirement for certified cost or pricing data.

(c) (1) Upon request of the Secretary of Defense, the Deputy Secretary of Defense, an Under Secretary of Defense, or the Deputy Under Secretary of Defense, Research and Engineering (Acquisition Policy), or outside the Department of Defense, of officials in equivalent positions, the Cost Accounting Standards Board may waive all or any part of the requirements of paragraph (a) of this section with respect to a national defense contract or subcontract. Any request for a waiver shall describe the proposed contract or subcontract for which waiver is sought and shall contain:

(i) An unequivocal statement that the proposed contractor or subcontractor refuses to accept a contract containing all or a specified part of the Cost Accounting Standards clause and the specific reason for that refusal, (ii) a statement whether the proposed contractor or subcontractor has accepted any prime contract or subcontract with any Federal department or agency containing the Cost Accounting Standards clause, (iii) the amount of the proposed award and the sum of all awards by the department or agency requesting the waiver to the proposed contractor or subcontractor in each of the preceding 3 years, (iv) a statement that no other source of the supplies or services being procured is available to satisfy the needs of the agency on a timely basis, (v) a statement of any alternative methods of fulfilling the project or program needs and the agency's reasons for rejecting such alternatives, (vi) a statement of the steps being taken by the procuring agency to establish other sources of supply for future procurements of the products or services for which a waiver is being requested, and (vii) any other information that may aid the Board in evaluating the requested waiver.

(2) Except as provided herein, the authority in paragraph (c)(1) of this section shall not be delegated. For any contract or subcontract for the procurement of substantially the same product or service from the same contractor for whom, pursuant to paragraph (c)(1) of this section, a waiver has previously been requested and granted by the Cost Accounting Standards Board, authority contained in paragraph (c)(1) of this section, may be delegated by the Secretary of Defense to the Secretaries of the Military Departments and to the Director, Defense Supply Agency, and by the heads of other agencies to officials in equivalent positions.

§ 331.40 [Reserved]

§ 331.50 Contract clause.

Except as provided in either § 331.30 or Part 332 of this chapter the clause set forth below shall be inserted in all negotiated national defense prime contracts and subcontracts.

COST ACCOUNTING STANDARDS

(a) Unless the Cost Accounting Standards Board has prescribed rules or regulations exempting the contractor or this contract from standards, rules, and regulations promulgated pursuant to 50 U.S.C. App. 2168 (Pub. L. 91-379, August 15, 1970), the contractor, in connection with this contract shall:

(1) By submission of a Disclosure Statement, disclose in writing his cost accounting practices as required by regulations of the Cost Accounting Standards Board. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the contractor and which contain a Cost Accounting Standards clause. If the contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets and commercial or financial information which is privileged and confidential, the Disclosure Statement will be protected and will not be released outside of the Government.

(2) Follow consistently his cost accounting practices in accumulating and reporting

contract performance cost data concerning this contract. If any change in cost accounting practices is made for purposes of any contract or subcontract subject to Cost Accounting Standards Board requirements, the change must be applied prospectively to this contract, and the Disclosure Statement must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) below, as appropriate.

(3) Comply with all Cost Accounting Standards in effect on the date of award of this contract or if the contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the contractor's signed certificate of current cost or pricing data. The contractor shall also comply with any Cost Accounting Standard which hereafter becomes applicable to a contract or subcontract of the contractor. Such compliance shall be required prospectively from the date of applicability to such contract or subcontract.

(4) (A) Agree to an equitable adjustment as provided in the changes clause of this contract if the contract cost is affected by a change which, pursuant to (3) above, the contractor is required to make to his cost accounting practices.

(4) (B) Negotiate with the contracting officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of this subparagraph (4): *Provided*, That no agreement may be made under this provision that will increase costs paid by the United States.

(4) (C) When the parties agree to a change to a cost accounting practice, other than a change under (4)(A) above, negotiate an equitable adjustment as provided in the changes clause of this contract.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if he or a subcontractor fails to comply with an applicable Cost Accounting Standard or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States together with interest thereon computed at the rate determined by the Secretary of the Treasury pursuant to Pub. L. 92-41, 85 Stat. 97, or 7 percent per annum, whichever is less, from the time the payment by the United States was made to the time the adjustment is effected.

(b) If the parties fail to agree whether the contractor or a subcontractor has complied with an applicable Cost Accounting Standard, rule, or regulation of the Cost Accounting Standards Board and as to any cost adjustment demanded by the United States, such failure to agree shall be a dispute concerning a question of fact within the meaning of the disputes clause of this contract.

(c) The contractor shall permit any authorized representatives of the head of the agency, of the Cost Accounting Standards Board, or of the Comptroller General of the United States to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The contractor shall include in all negotiated subcontracts which he enters into the substance of this clause except paragraph (b), and shall require such inclusion in all other subcontracts of any tier, including the obligation to comply with all Cost Accounting Standards in effect on the date of award of the subcontract or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed certificate of current cost or pricing data. This requirement shall apply only to negotiated subcontracts in excess of $100,000 where the price negotiated is not based on:

(1) Established catalog or market prices of commercial items sold in substantial quantities to the general public, or

(2) Prices set by law or regulation, and except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a Cost Accounting Standards clause by reason of § 331.30(b) of Title 4, Code of Federal Regulations (4 CFR 331.30(b)).

§ 331.51 Findings.

Prior to the utilization of the provisions of paragraph (a)(4)(C) of the contract clause set out in § 331.50(b), the contracting officer shall make a finding that the change is desirable and is not detrimental to the interests of the Government.

§ 331.60 Disclosure requirements.

General provisions concerning filing of a Disclosure Statement and the time at which such Disclosure Statement must be filed are set forth in Part 351 of this chapter.

§ 331.70 Interpretation.

(a) Increased costs paid by the United States as referred to in the Cost Accounting Standards clause in § 331.50 shall be deemed to have resulted whenever the cost paid by the Government results from a change in a contractor's cost accounting practices or from a failure to comply with applicable Cost Accounting Standards, and such cost is higher than it would have been had the practices not been changed or applicable Cost Accounting Standards been complied with.

(b) If the contractor under any fixed price contract, including a firm fixed price contract, fails during contract performance to follow his cost accounting practices or to comply with applicable Cost Accounting Standards, increased cost paid by the United States under contracts containing the clause set forth in § 331.50(a) is measured by the difference between the contract price agreed to and the contract price that would have been agreed to had the contractor proposed in accordance with the cost accounting practices used during contract performance. The determination of the contract price that would have been agreed to will be left to the contracting parties and will depend on the circumstances of each case.

(c) The statutory requirement underlying this interpretation is that the United States not pay increased costs, including a profit enlarged beyond that in the contemplation of the parties to the contract when the contract costs, price, or profit is negotiated, by reason of a contractor's failure to use applicable Cost Accounting Standards or to follow consistently his cost accounting practices. In making price adjustments under the Cost Accounting Standards clause in § 331.50, in fixed-price or cost-reimbursement incentive contracts, or contracts providing for prospective or retroactive price redetermination, the Federal agency shall apply this requirement appropriately in the circumstances.

(d) The contractor and the contracting officer may enter into an agreement as contemplated by paragraph (a)(4)(B) of the Cost Accounting Standards clause in § 331.50, covering a change in practice proposed by the Government or the contractor for all of the contractor's contracts for which the contracting officer is responsible, provided that the agreement does not permit any increase in the cost paid by the Government. Such agreement may be made final and binding, notwithstanding the fact that experience may subsequently establish that the actual impact of the change differed from that agreed to.

(e) To facilitate agreements with a contractor who has a large number of contracts affected by a proposed change in his cost accounting practices or affected by application of Cost Accounting Standards, contracting agencies are urged to establish procedures under which the contractor may seek, and in proper cases obtain, agreement with a single official concerning the impact of the proposed change or application of standards upon all such contracts of the agency.

(f) An adjustment to the contract price or of cost allowances pursuant to the Cost Accounting Standards clause in § 331.50 may not be required when a change in cost accounting practices or a failure to follow Standards or cost accounting practices is estimated to result in increased costs being paid under a particular contract by the United States. This circumstance may arise when a contractor is performing two or more covered contracts and the change or failure affects all such contracts. The change or failure may increase the cost paid under one or more of the contracts, while decreasing the cost paid under one or more of the contracts. In such case, the Government will not require price adjustment for any increased costs paid by United States so long as the cost decreased under one or more contracts are at least equal to the increased cost under the other affected contracts, provided that the contractor and all affected contracting officers agree on the method by which the price adjustments are to be made for all affected contracts. In this situation, the contracting agencies would, of course, require an adjustment of the contract price or cost allowances, as appropriate, to the extent that the increases under certain contracts were not offset by the decreases under the remaining contracts.

§ 331.71 Materiality.

(a) In determining whether amounts of cost are material or immaterial, the following criteria shall be considered where appropriate; no one criterion is necessarily determinative.

(1) The absolute dollar amount involved. The larger the dollar amount, the more likely that it will be material.

(2) The amount of contract cost compared with the amount under consideration. The larger the proportion of the amount under consideration to contract cost the more likely it is to be material.

(3) The relationship between a cost item and a cost objective. Direct cost items, especially if the amounts are themselves part of a base for allocation of indirect cost, will normally have more impact than the same amount of indirect costs.

(4) The impact on Government funding. Changes in accounting treatment will have more impact if they influence the distribution of costs between Government and non-Government cost objectives than if all cost objectives have Government financial support.

(5) The cumulative impact of individually immaterial items. It is appropriate to consider whether such impacts (i) tend to offset one another, or (ii) tend to be in the same direction and hence to accumulate into a material amount.

(6) The cost of administrative processing of the price adjustment modification shall be considered. If the cost to process exceeds the amount to be recovered, it is less likely the amount will be material.

(b) (1) A contract modification for price adjustment or cost allowance under the Cost Accounting Standards clause is required only if the cost impact is material.

(2) Where a contractor is in noncompliance and does not change a cost accounting practice because the cost impact is immaterial, the contracting agency is not relieved of its responsibilities to assure that an appropriate price adjustment is obtained if the cost impact of the noncompliance subsequently becomes material. The contractor shall be notified that the Government's decision to forbear action for noncompliance is solely because the cost impact at the time of the notice is immaterial. If at any time thereafter, the Government determines that the cost impact of noncompliance with respect to the practice in question is material, the Government then must require action under paragraph (a)(5) of the contract clause set forth in § 331.50 for any cost accounting period in which the cost impact is material. The fact that the Government does not pursue a price adjustment does not excuse the contractor from his obligation to comply with the Standard involved.

(3) Whether cost impact is recognized by modifying a single contract, several but not all contracts, or all contracts, or any other suitable technique, is a contract administration matter. The Standards, rules, and regulations of the Board do not in any way restrict the capacity of the parties to select the method by which the cost impact attributable to a change in cost accounting practice is recognized.

§ 331.72 Relationship to Part 332.

Contracts subject to this part may be performed during a cost accounting period in which a previously awarded contract subject to Part 332 of this chapter is also being performed. Compliance with the requirements established by this part may compel the use of cost accounting practices for contracts covered by this part that are not required under Part 332 of this chapter. Under these circumstances, the cost accounting practices applicable to contracts subject to Part 332 of this chapter need not be changed. Any resulting differences in practices between the contracts subject to this part and those subject to Part 332 of this part shall not constitute violations of Standard 401 or 402.

§ 331.80 Effective date.

Part 331, as amended, must be applied to contracts with a date of award after April 1, 1981, or if the contractor has submitted cost or pricing data, with a date of final agreement on price after that date.

PREAMBLE A

Preamble to Original Publication, 2-29-72

The material set forth below is the preamble to the original publication of Part 331, February 29, 1972, at 37 FR 4139. For the preamble to the republication of Part 331 (November 7, 1973, 38 FR 37025), see preamble D of this Supplement. Portions of this preamble relating to Parts 351, 400, and 401 have been omitted; they can be found in the supplements to their respective parts. This preamble to the publication of February 29, 1972, is included as part of the administrative history of Part 331.

General comments. The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C. app. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives—improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable, representatives of various Government agencies, Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, FEDERAL REGISTER for comment.

To better assure that all who might want to comment had an opportunity to do so, the Board supplemented the FEDERAL REGISTER notice by sending copies of the FEDERAL REGISTER materials directly to about 175 organizations and individuals who had expressed interest or had provided assistance in the development of the published material. Also, a press release was distributed announcing the publication, which resulted in numerous articles in journals. The Board availed itself of all opportunities to publicize the proposals and solicit comments on them.

Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry associations public accounting firms, individual companies, and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board's disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

1. *Public availability of disclosure statement.* In a special notice in the notice of proposed rule making, the Board sought comments to assist it in its determination of whether Disclosure Statements submitted by defense contractors and subcontractors should be available to the general public, pursuant to the Public Information Section of the Administrative Procedure Act (5 U.S.C. 552) or whether such information was properly within one of the statutory exceptions to the legal requirement for public availability.

With few exceptions, both Government and industry commentators urged that the Disclosure Statements not be made available to the general public. Numerous arguments were presented. Among them were that public disclosure by a Government official would violate 18 U.S.C. 1905 (a provision in the Criminal Code making it a crime for a Government official to make certain matters public in certain circumstances), thus making disclosure improper under an exception to the requirement for public availability set out in 5 U.S.C. 552(b)(3); that the cost accounting practices were trade secrets or property of considerable value and that disclosure would deprive the company of their value without compensation; that disclosure would reduce competition; and that the public might be misled in that it might construe disclosures respecting the defense segment of a contractor's business as representative of his entire business organization.

An argument in favor of making the Disclosure Statements available to the public was made by a public interest group. It argued that 5 U.S.C. 552 clearly applies to Disclosure Statements, which do not fall within any exception to public availability; that the public requires access to Disclosure Statements in order to consider adequately and comment intelligently on any Cost Accounting Standards proposed by the Board; that public availability would enhance competition; that Disclosure Statements which are ultimately approved will form a body of precedents to guide others in complying with future Board Standards and that public availability will enable citizens and the Congress to hold both the Board and contracting officials accountable for implementation of section 719. A few commentators stated that they favored, or could see no harm to companies from, public availability of contractors' disclosed practices.

The Board is especially impressed with arguments that cost accounting practices have never been made public, that companies have regarded and treated them as confidential, and that a company's competitive position would be damaged by public disclosure of its cost accounting practices. Since disclosure will be required of many companies or divisions of companies whose principal competitors are not subject to Board regulations, the Board recognizes there might arise competitive disadvantage to the disclosing company or division if its competitors may see its disclosure but need make none themselves. The Board has, in light of these latter arguments, concluded that information received in response to Disclosure Statements is within the exception set forth at 5 U.S.C. 552(b)(4) and that the Board will not make Disclosure Statements public in any case when the company or segment files its statement specifically conditioned on the Government's agreement to treat the Disclosure Statement as confidential information.

A provision to this effect has been added at § 351.4(d) of Part 351. Additionally, paragraph (a)(1) of the contract clause set forth at § 331.5 has been modified to this effect, and a provision added to it so that subcontractors may submit Disclosure Statements directly to the contracting officer.

While the Board has concluded that public availability of the Disclosure Statements of identified contractors is not required, it will, nevertheless, implement its announced intention of

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compiling statistical summaries of disclosure data and making those studies available to the public. The Board believes that the creation of a data bank of cost accounting practices will greatly benefit the Board's own research efforts and the formulation of Cost Accounting Standards; summaries of these data or studies of them should also prove to be of great value to the public. Aggregated information not identified to particular contractors will, therefore, be made available to the public.

2. *Contractor-subcontractor relationships.* Several commentators, stating that contractors cannot dictate the cost accounting practices of their subcontractors at any tier, urged that the Board not hold contractors responsible for increased costs to the United States arising from the failure of subcontractors to follow Cost Accounting Standards or disclosed cost accounting practices. Several commentators also urged that the contractor not be subject to the possibility of a default termination by reason of the actions or inactions of any of its subcontractors at any tier. Finally, some commentators urged that the Board establish a novel concept of privity between the contracting agency and subcontractors with respect to any concerns stemming from Board rules, regulations, and Cost Accounting Standards.

The Board has dealt with many of the issues touched on by these commentators in its conclusions, discussed below, respecting the phasing of applicability and the proposed termination-for-default language in the Contract Clause. The Board is also mindful of the desirability of its maintaining neutrality with respect to contracting policies outside its jurisdiction; thus it should avoid establishing a standard or policy which would influence decisions of whether work should be performed in-house or subcontracted. A Board policy permitting contractors to avoid responsibility for the actions of their subcontractors could surely have such an impact.

The Board reaffirms the established principle that prime contractors are responsible to the Government for performance of their contracts in all required respects and urges that contractors who are fearful of deficiencies in their subcontractors' performances protect themselves by use of whatever means they currently employ under other flow-down contractual requirements.

3. *Exemptions.* Many commentators urged the Board to provide exemptions either to the requirement to file a Disclosure Statement or to both that requirement and the requirement to follow Cost Accounting Standards. Exemptions were urged for subcontractors below the first tier, subcontractors with small amounts of defense contracting business, producers of basic or raw materials, colleges and universities, construction contractors, firms which would qualify as small businesses, and others.

The Board has long been concerned with the question of appropriate exemptions. It has specifically requested interested groups to offer suggestions for criteria for use by the Board in considering exemptions. It also requested its staff to study exemptions and has discussed the staff investigations at Board meetings. In light of these studies and the comments received, the Board has found no persuasive reasons for issuing blanket or class exemptions at this time.

The Board recognizes, however, that individual Cost Accounting Standards may by their nature be inapplicable or inappropriate to certain classes or categories of defense contractors or contracts. The Board will continue to consider exemptions from individual proposed Cost Accounting Standards as appropriate.

With respect to the requirement to submit a Disclosure Statement, the Board's proposed regulation provides a phasing of that requirement. The Board remains convinced that a company which together with its subsidiaries received prime contract awards of negotiated national defense contracts including supplemental awards during Federal fiscal year 1971 totaling more than $30 million should be required to submit a Disclosure Statement as soon as Part 351 of the Board's regulations becomes effective. In order to provide both to other contractors and to Government agencies adequate time within which to study the use of Disclosure Statements, however, the Board will defer determination of the date after which other affected contractors and subcontractors may be required to file Disclosure Statements. From time to time, the Board will announce the dates of applicability to other contractors and subcontractors.

4. *Applicability date of standards, rules, and regulations.* A related issue raised by many commentators is a request that Cost Accounting Standards be made applicable 90 days after issuance or at the beginning of the contractor's next fiscal year, whichever is later. In order to provide the maximum benefits from use of Cost Accounting Standards, the Board has decided not to adopt any rule which would automatically delay the effective date of Cost Accounting Standards beyond the dates contemplated in section 719(h). That section provides a minimum of 4 months' notice from the date of promulgation, to contractors of the likely applicability of a Cost Accounting Standard. The Board regards this as an adequate time for companies to prepare for use of the standard. The Board nevertheless recognizes that certain standards by their nature may require deferring applicability to the beginning of a contractor's fiscal year next following the effective date, and in such cases that applicability will be stated in the standards concerned.

5. *Agency administrative responsibility.* Many commentators, noting the Board's statutory responsibility to promote uniformity and consistency in cost accounting practices used in defense contracting and subcontracting, have suggested that uniformity would be promoted by giving the Board or another single Federal agency the sole implementing responsibility respecting Board regulations. Thus, some commentators recommended that the Board itself issue regulations prescribing the frequency of submission of Disclosure Statements and where they must be submitted. Other commentators urged that the Board issue a single regulation prescribing exact methods by which increased costs to the United States will be determined. Other commentators urged that the Board prescribe methods by which advance agreements affecting more than one contract shall be made, some commentators urging that the Board itself make those agreements. Others urged that the Board rule that the contracting agencies must act to approve or disapprove Disclosure Statements within a stated period of time. And finally, some commentators urged that the Board itself be the sole agency to approve the cost accounting practices disclosed through submission of a Disclosure Statement.

The Board finds these recommendations cogent. It also recognizes that to act pursuant to them would require a Board regulation directed to the administrative and contracting procedures of many Federal agencies and in some cases—such as the recommendation for Board approval of disclosed cost accounting practices—substitute a Board regulation for the exercise of contracting officers discretion.

The Board, therefore, has decided not to implement at this time the suggestions set forth in this connection. The Board nevertheless will watch closely during the early implementation by contracting agencies of Board rules, regulations, and Cost Accounting Standards so that it may become aware of any diversity of regulations or actions by contracting agencies. If the Board finds that an unacceptable amount of diversity has arisen, it will be prepared to reconsider the recommendations that the Board issue its own regulations in many of the areas left by Board regulations to the discretion of contracting agencies.

Many commentators have expressed concern about the problems which could arise from inconsistent actions by different Federal agencies respecting disclosed practices, changes in practices, and equitable adjustment of contract prices and costs. The Board has directed its staff to work with representatives of relevant Federal agencies with the objective of obtaining designation of a single contracting officer for each contractor or major component thereof in order to achieve consistent practices within the standards issued by the Board.

6. *Contract modifications.* Several commentators have urged that negoti-

ated contract changes and amendments over $100,000 to contracts which are themselves not subject to Board jurisdiction should not be covered. One commentator pointed out that in a long-term contract, most changes represent "instead of" type changes with cost of price adjustments only for the incremental effect of the change. This commentator stated that there is no practical way separately to identify these incremental costs.

The Board is persuaded that for the time being it should not cover negotiated modifications to contracts exempt at their inception. It has therefore, eliminated coverage for the time being of such contract modifications. In doing so, however, the Board intends that the annual extension of existing negotiated contracts and similar contract modifications would not be exempt from the Board's rules, regulations, and Cost Accounting Standards.

7. *Definitions.* The Board is also persuaded of the value of one commentator's suggestion that the Board provide a compilation of definitions of the words or phases defined in individual Cost Accounting Standards, making those definitions applicable to all such standards. Consequently, a new Part 400 has been added, and all terms defined in Parts 401 and 402 have been placed in it, although they also remain in the particular standards in which they are defined. As more standards are added, any terms defined in them will also be added to Part 400. However, terms defined in Parts 331 and 351 are not included in the glossary of definitions, nor are terms used in those parts necessarily to bear the meanings ascribed to those terms in Part 400.

8. *Application to individual contracts.* Several commentators urged that the Board adopt the date of final agreement on a negotiated price as a cut-off date for the disclosure of cost accounting practices. The Board has reviewed the merits of selecting that date rather than the date of award to establish the date as of which the contractor's Disclosure Statement must accurately reflect his cost accounting practices, at least with respect to those contracts where cost or pricing data have been submitted pursuant to Pub. L. 87-653. The Board has decided to use the date of final agreement on price, as shown on the signed certificate of current cost or pricing data, with respect to contractors who have submitted cost or pricing data, and to use the date of award of the contract for all other contractors. In addition, the Board has concluded that it is appropriate to use those dates to establish which Cost Accounting Standards shall be applicable to the proposal and to the contract at its inception. Appropriate changes in Parts 331, 351, and 401 have been made to reflect this decision.

9. *Price adjustments.* Many commentators stated that where a contractor's departure from existing disclosed practices is occasioned by the contractor's wish to adopt a newly issued Cost Accounting Standard for all contracts, the Government should be willing to provide upward price adjustment whenever an existing contract is rendered thereby more expensive to perform. The view was often expressed that contractors could not maintain one accounting practice for contracts subject to a particular Cost Accounting Standard, but a different practice for contracts not so subject; therefore, it was alleged, once a contractor had to adopt a standard for any one contract, he would of necessity adopt it for all contracts and amend his Disclosure Statement accordingly.

The Board notes in this connection that the Cost Accounting Standard at Part 402 requires consistency in the allocation of all direct and indirect costs under all covered contracts. If a Cost Accounting Standard were issued which required a company to modify its disclosed cost accounting practices with respect to its earlier practice of allocating direct and indirect costs, Part 402 would require emendment of existing disclosed practices so as to meet that requirement. In such a case, the Board believes it would be unfair to deny an equitable price adjustment arising from such amendment.

Further, the Board has been persuaded by the strong arguments from industry commentators that companies with more than one contract, subject to different Cost Accounting

Standards, cannot maintain multiple records to account for each contract related to its set of standards. Another industry commentator stated that the vast majority of companies must apply any required cost accounting practices across their total business, and that it would be impractical if not impossible for companies to apply different practice to different contracts.

The Board has accommodated this view by enabling contractors to apply uniform practices to all covered contracts. Such application will also serve to improve cost accounting practices for all contracts.

The Board has consequently modified both Part 331 and Part 351 to provide three things: First, that a contractor's practices disclosed for any contract shall be the same as the practices currently disclosed and applied on all other covered contracts and subcontracts being performed by that contractor. Second, that a contractor must amend his disclosure of cost accounting practices as new standards are issued and become applicable to new contracts if a change in practices is necessary, so that, at any given time, the same practices prevail under all of the contractor's existing contracts and subcontracts subject to Board jurisdiction. Similarly, contractors must amend Disclosure Statements to reflect any change in practices disclosed under later contracts. Third, that for those amendments of disclosed practices applicable to a particular contract which are occasioned by the issuance of a new Cost Accounting Standard, the Government will equitably adjust the contract price in accordance with the changes clause in the contract or reimburse any increased costs under that contract.

In view of the phasing of the requirement to file a Disclosure Statement, the Board has adopted a contract provision that will provide equitable adjustments in appropriate cases when a contractor who has not yet filed a Disclosure Statement is required to change his established cost accounting practices to comply with newly issued Cost Accounting Standards. On the other hand, any departure from disclosed cost accounting practices which is not required by a newly issued Cost Accounting Standard will not be subject to equitable price adjustment, but only to price adjustment downward in the event that that departure would otherwise result in increased costs being paid by the United States. The Board wishes to emphasize that if the parties to a contractual negotiation mutually agree to a price based on exclusion of costs which are allocable under the contractor's disclosed cost accounting practices, such agreement shall not affect the requirement for conformity with Board rules, regulations, and Cost Accounting Standards in the contractor's allocation of costs between the contract being negotiated and other work.

10. *Materiality.* The Board notes that many commentators urged that a concept of materiality be incorporated in the Board's regulations, to the end that minimal or insignificant modifications of or failures to use disclosed cost accounting practices would not be subject to price adjustment.

The Board agrees that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. Since this rule of common sense is already practiced by the Government, the Board does not believe that there is any need to attempt to formulate and state in acceptable concept of materiality applicable to all Board rules, regulations, and standards, although the Board might consider doing so if subsequent events indicate the necessity therefor. The Board does recognize that in particular standards a "materiality" statement may be useful, and in such cases, it will include one. See for example the addition at § 402.50(e).

11. *Additional requirements by agencies.* As a final general point, concern was expressed that Federal agencies might require submission of cost proposals in ways inconsistent with the cost accounting practices of some or all of the potential offerors. The Board recognizes that this has happened in the past, but it notes that Board rules, regulations, and Cost Accounting Standards are to be used by relevant Federal agencies as well as by contractors and subcontractors, and it believes that henceforth requests for

proposals must be fully consistent with such rules, regulations, and standards, although of course the Federal agency may ask for supplementary information to accompany proposals if this is needed to meet the agency's requirements.

OTHER COMMENTS

Section 331.2 Definitions. A few commentators recommended modifying the definition of "relevant Federal agency." Their purpose was to assure that agencies such as the General Accounting Office and the Renegotiation Board were excluded from the definition of such agencies. Those recommendations have not been accepted, since the Board believes the General Accounting Office, the Renegotiation Board, and other agencies whose responsibilities include review, approval, or other action affecting national defense procurements are within the meaning of "relevant Federal agencies."

One Federal agency urged that the definition of "national defense" be supplemented at the end by adding the phrase "including R. & D. and services." The Board believes this addition unnecessary, in light of the definition at § 331.2(b) of "defense contractor," and the definition of "material" set out in 50 U.S.C. App. 2152 as including "technical information." The Board, of course, agrees that contractors for research and development as well as other services are national defense contractors in light of these definitions.

Several commentators urged that the definition of "negotiated subcontract" at § 331.2(f) be broadened to reflect what the commentators believed was the Board's purpose in this definition, that of precluding jurisdiction over subcontracts made after adequate price competition. That is not the Board's intention; instead, the Board intended to exclude from the term "negotiated subcontract" only a subcontract made under conditions which are as close to the conditions governing Federal advertised contracts as possible. Accordingly, the Board has not accepted these suggestions, but it has added language to clarify its intention.

In connection with this comment, the Board notes that several commentators urged that the Board exempt altogether from its jurisdiction any contract made after adequate price competition. The Board believes that any such exemption would be unwarranted and undesirable in view of the legislative history of section 719.

Section 331.5 Contract clause. The major changes in the contract clause urged by commentators have already been discussed in points 2 and 9 of the discussion of general comments. Commentators raised a number of additional points with respect to this contract clause. A great many commentators objected to the provision in paragraph (e) for termination for default. Many commentators urged that the requirement to repay increased costs to the United States should be deemed the sole remedy for a refusal or failure to comply with the requirements of the contract clause. While that remedy may be adequate for almost all cases involving a failure to follow Cost Accounting Standards or disclosed cost accounting practices, it would not be adequate to meet other possible situations, where, for example, a contractor refused to make a post-award submission of a Disclosure Statement or refused to grant access to records as required by the contract clause. In view of the fact that breach of any of the requirements of this clause would be a breach of a material condition of the contract, the default clause generally applicable to performance of the contract provides adequate coverage. Consequently, the Board has deleted the specific termination language in this contract clause as requested by many commentators.

Some commentators urged deletion or modification of paragraph (c) of the contract clause, which the Board has not done, since that language is prescribed by section 719(j). Other commentators urged that the Board set forth a specific period during which contractor and subcontractor documents, papers, or records relating to compliance with Cost Accounting Standards must be retained. The Board believes that there is no need to do so, since the general records retention requirements of any particular contract will establish that period.

One Federal agency requested that the disputes language in paragraph (d) be modified to accommodate that agency's practice of permitting subcontractors to bring contract disputes directly to that agency's Board of Contract Appeals. The Board has accepted this recommendation. Two Federal agencies recommended deletion of the definitions in this contract clause as unnecessarily duplicating § 331.2. The Board agrees and has made the deletion, except that the definition of "negotiated subcontractor" has been retained in the contract clause for the convenience of contractors and subcontractors.

Other suggestions were received in which the Board was urged to modify other language in the contract clause which is taken directly from provisions in section 719. Preferring to use the statutory language, the Board has not accepted these suggestions. It has however, modified its proposal in paragraph (b) so as to adopt the statutory language, as urged by one commentator.

Section 331.6 Post award disclosure. Two Federal agencies urged that the contracting agencies be authorized to make awards whenever the head of the agency concluded that it was impractical to secure a Disclosure Statement from a contractor or from a subcontractor. Recognizing that any avoidable delays in making procurements are undesirable, the Board has accepted this recommendation. The Board does not expect that the authority thus provided to agency heads will be abused, and it will be informed of all actions taken pursuant to this authority.

* * * * *

Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in § 331.8, § 351.4(e), and Parts 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules or regulations.

1. The provisions of § 331.4 are to be included in all solicitations issued on or after July 1, 1972, which are likely to lead to contracts covered by standards, rules, and regulations of the Cost Accounting Standards Board.

2. The provisions of § 331.5 are to be included in all contracts resulting from solicitations covered by 1 above. In addition, these provisions are to be included in any other contract which is within the jurisdiction of the Cost Accounting Standards Board and which is awarded after October 1, 1972.

3. The provisions of Part 351 will be applicable to any contractor who submits a proposal which results in contracts containing the clause in § 331.5 and whose net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaled more than $30 million. Contractors whose net awards were less than that amount may be required to complete or submit a Disclosure Statement as the Board announces extensions of this requirement to such contractors.

4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

PREAMBLE B

Preamble to Amendment of 6-29-72

This amendment redesignated § 331.3 as § 331.3(a) and added a new § 331.3(b). The preamble and amendment were published on June 29, 1972, at 37 FR 12784. Although Part 331 was subsequently republished and revised on November 7, 1973 (38 FR 30725), the preamble to the amendment of June 29, 1972, is included as part of the administrative history of the regulation.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to § 331.3, *Applicability*, of its rules and regulations. The modification adopted today was initially published in the FEDERAL REGISTER of May 23, 1972 (37 FR 10454). Comments regarding that notice of proposed rulemaking were invited to be submitted to the Board by June 23, 1972.

The prescribed period has passed, and no comment opposing the proposed modification has been received. In view of this and for the reasons set forth on May 23, 1972, FEDERAL REGISTER, modification to § 331.3 of the Board's rules and regulations is adopted and made effective on July 1, 1972.

PREAMBLE C

Preamble to Amendments of 2-13-73

This amendment adds a new paragraph (c) to § 331.3, and deletes § 331.6(c). The preamble and amendments were published on February 12, 1973, at 38 FR 4237. Although Part 331 was subsequently republished and revised on November 7, 1973 (38 FR 30725), the preamble to the amendment of February 12, 1973, is included as part of the administrative history of Part 331.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. The modification was published initially in the FEDERAL REGISTER of December 8, 1972 (37 FR 26127). Some of the material in the modification was also published in the FEDERAL REGISTER of October 6, 1972 (37 FR 21177). Comments regarding the publication on December 8 were invited to be submitted to the Board by January 15, 1973.

The Board received 14 comments from a wide range of commentators. The Board is grateful for their interest and takes this occasion to thank them for the comments.

One commentator urged the Board to require certain additional information to support waiver applications pursuant to paragraphs (1)(i), (1)(iii), and (2)(i) of § 331.3(c). The Board agrees that such additional information will assist it in deciding whether to grant a waiver and therefore has adopted this proposal.

Two commentators urged that the signed, unequivocal statement by a proposed contractor or subcontractor that it refuses to accept a contract containing the Cost Accounting Standards clause might not be obtainable even when there has been such a refusal. The Board agrees and has consequently modified the requirement at § 331.3(c)(1)(i) so that the agency's statement of the fact of an unequivocal refusal, and of the contractor's or subcontractor's specific reasons therefor, will be sufficient to satisfy this requirement.

A commentator suggested that the Board provide for exemption from particular portions of the Cost Accounting Standards clause, as well as providing for exemption from all of it. The Board agrees that it is helpful to spell out such authority and has modified its proposal accordingly.

The Honorable Wright Patman, Chairman of the Committee on Banking and Currency of the House of Representatives, noting that any extensive use of the Board's proposed authority could seriously weaken the objectives of section 719 of the Defense Production Act of 1950, as amended, requested that within 30 days after acting on any request for an exemption the Board transmit to him a full report of the exemption request and its action thereon. The Board is pleased to comply with this request. A similar report will also be submitted to the Chairman of the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate.

Another commentator urged in the interest of assuring maximum access by the public and the Congress to the Board's actions that requests for waivers be published in the FEDERAL REGISTER and that comments on them be solicited that the Board's action on a request and an explanation of it be published in the FEDERAL REGISTER, and, finally, that notwithstanding any prior publication, that the Board include in its annual report to Congress a listing of every request for waivers received during the year, together with an explanation of the Board's action granting or denying the request. This commentator, asserting that the Board does not have unlimited discretion to grant waivers or exceptions, urges that the standards the Board will apply in acting on requests for waivers be stated.

The Board adopts the suggestion that it include in its annual reports to Congress a listing of the requests it receives for waivers and its disposition of those requests. The Board, however, does not believe that it should publish a notice of requested waiver and solicit comments. As noted above, the Board will provide full information to the Congress and to the public through its reports on its actions on waivers. With respect to this commentator's suggestion that the Board publish the criteria which it will use in acting on requests for waivers, the Board is satisfied that those criteria clearly are implicit in the information which the Board is requiring to be submitted in support of a request for a waiver.

Several commentators urged that the Board delegate its waiver authority to the procuring agencies, stating essentially that waivers could thus be granted more expeditiously. The Board has not accepted this suggestion, since it believes that it should retain control over a matter as important as a total exemption from the requirements of section 719 of the Defense Production Act of 1950, as amended, and also because the Board is convinced that its retention of its waiver authority will not unduly delay action on waiver requests. In this connection, the Board reemphasizes its comments published in the FEDERAL REGISTER for December 8, 1972 (37 FR 26127) that, "The Board * * * is prepared to act promptly in response to requests for waivers but * * * the Board's ability to respond promptly will depend in very large measure on whether or not the agency's request for a waiver is in full accord with the proposed requirements." If experience shows that delegation of this authority is warranted, the Board will, however, reconsider this suggestion.

Some of these commentators also urged that the level of agency officials authorized to submit requests for waivers to the Board be modified to include persons at levels of responsibility below those indicated in the Board's proposal. The Board believes that the level proposed will not unduly burden the procuring agencies and will assure that any request for a waiver of the Board's regulations will receive consideration at a very high level within the procuring agency before submission to the Board. It, therefore, does not adopt this suggestion at this time, although it may reconsider this suggestion if experience warrants.

Some commentators urged the Board to expand its proposal to permit exemptions on broader bases, instead of confining the exemption authority to particular cases of demonstrated need. The Board does not accept this suggestion, since it does not anticipate wholesale or, indeed, even very numerous requests for waivers. Nevertheless, should a need for broader exemption action be justified, the Board can deal with that need under its authority in section 719(h)(2) of the Defense Production Act of 1950, as amended.

One commentator urged an outright exemption for both foreign and domestic concerns for work performed outside the United States, and other commentators urged the exemption of all subcontracts performed in Canada. The Board has adopted neither of these proposals, since it believes that the arguments advanced for them are unpersuasive in light of the purposes of section 719. The Board believes, further, that the exemption authority being adopted today provides an adequate basis for waivers where they are appropriate.

A commentator is concerned that the phrase, "on a timely basis," in §§ 331.3(c)(1)(iv) and 331.3(c)(2)(iv), if given a narrow interpretation, might suggest that timeliness of delivery is the only condition for granting a waiver. That commentator points out that other conditions also may warrant consideration. The Board agrees with the commentator, but it does not believe that a modification of its proposal is necessary to avoid the narrow interpretation feared.

In the interest of clarity, the waiver provision in § 331.6(c) is deleted from that section and transferred to § 331.3(c).

The Board has revised its proposal as discussed above and has made minor technical improvements. The revised proposal is adopted today.

PREAMBLE D

Preamble to Republication, 11-7-73

This publication (38 FR 30725, Nov. 7, 1973) revised and republished Part 331.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the FEDERAL REGISTER of September 5, 1973 (38 FR 23971). The amendments:

(a) Renumber Parts 331 and 351 to facilitate insertion of future modifications to those parts; (b) clarify one section of the contract clause at § 331.5; and (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various Parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973:

PREAMBLE E

Preamble to Amendment of 9-19-74

This amendment revised paragraph (c)(4) of § 331.30, and was published on September 19, 1974, at 39 FR 33681.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. The modification adopted today was initially published in the FEDERAL REGISTER of August 9, 1974 (39 FR 28645). Comments regarding that notice of proposed rulemaking were invited to be submitted to the Board by September 9, 1974.

The August 9, 1974, publication proposed an amendment to § 331.30(c)(4) to permit, under certain circumstances, submission of waiver requests from a level below that of the agency head. No objection to the Board's proposal has been made. Therefore, the proposal has been adopted for the reasons expressed in the August 9, 1974, publication.

PREAMBLE F

Preamble to Amendments of 12-24-74

This document amended § 331.30(a), added § 331.30(b)(8), and amended §§ 331.40 and 331.50. It was published Dec. 24, 1974, at 39 FR 44389.

The purpose of this publication by the Cost Accounting Standards Board is to adopt modifications to Part 331, Contract Coverage, and Part 351, Basic Requirements, of its rules and regulations. These modifications will provide an exemption from Cost Accounting Standards Board requirements for certain national defense contracts and subcontracts of $500,000 or less.

Public Law 91-379 requires that Cost Accounting Standards must be used in all negotiated prime contract and subcontract national defense procurements with the United States in excess of $100,000, with certain stated exceptions. From time to time the Board refers to contracts subject to its rules and regulations as "covered contracts". Section 719(h)(2) of Pub. L. 91-379 authorizes the Cost Accounting Standard Board to prescribe rules exempting from its requirements such classes or categories of national defense contractors and subcontractors as it determines, on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to be achieved by Pub. L. 91-379. The Board has granted several exemptions to classes or categories of contractors and subcontractors and also has established a procedure under which waiver of the Board's requirements may be granted for individual contracts.

A proposed exemption increasing the minimum contract amount requiring compliance with Cost Accounting Standards Board rules, regulations and Standards from $100,000 to $500,000 was published by the Board on September 27, 1974 (39 FR 34669). The Board received 82 responses to the September 27 proposal. Comments were received from individual companies, government agencies, professional associations, industry associations, public accounting firms, and individuals. All of these comments have been carefully considered by the Board, and the Board takes this opportunity to express its appreciation for the helpful suggestions which have been furnished.

The comments below summarize the major issues discussed by respondents in connection with the initial publication and explain the Board's disposition of these issues.

Issuance of the exemption. Practically all the commentators expressed concurrence in the proposed exemption, giving either unqualified support or support with added comments that additional exemptions should also be considered. However, three commentators—a consulting firm, a major aerospace company and a Government agency—disagreed with the proposed exemption, stating that an increase in the threshold for compliance with CAS requirements was inconsistent with the Board's objective of establishing uniformity and consistency among contractors doing business with the Government.

The Board agrees that the adoption of the proposed regulation will exempt a substantial number of contractors and subcontractors who otherwise would be covered, and consequently will permit such companies to follow accounting practices other than those set out in Cost Accounting Standards. However, the Board is aware that compliance with its rules, regulations and standards may involve additional administrative effort, particularly on the part of small companies, which may not be commensurate with the benefit to the Government or the contractor resulting from such compliance. The Board, after considering the efforts required by both the Government and its contractors to assure compliance on all covered contracts in excess of $100,000, is persuaded that maximum benefit to the Government with minimum cost can be achieved by limiting the mandatory application of its standards to contractors who receive awards which constitute a substantial majority of the national defense procurement dollars. As was stated at the time the proposed exemption was issued for comment, some 70 percent of the prime contractors of the Department of Defense did not receive one or more negotiated awards in excess of $500,000 in Fiscal Year 1973. Thus, only 30 percent, or approximately 750 prime contractors, who received contract awards totaling $20 billion, would continue to be covered. The exemption would remove coverage from only about 10 percent of the dollar value of annual DOD awards.

In view of the foregoing, the Board considers the proposed exemption increasing the minimum contract amount requiring compliance with the Cost Accounting Standards Board rules, regulations, and standards to be in keeping with the purposes sought to be achieved by Pub. L. 91-379 and to be an appropriate exercise of the authority granted to the Board by section 719(h)(2) of that law.

Increase exemption on all contracts to $500,000. A number of commentators suggested that the $500,000 single contract threshold for compliance with Board rules, regulations, and standards be changed to exempt all contracts of $500,000 or less. Those giving reasons in support of this suggestion generally based their comments on simplification of administration. These commentators felt that it would be difficult for the Government or prime contractors, when awarding a prime contract or subcontract in excess of $100,000 to determine whether the contractor or subcontractor had in existence a prior $500,000 covered contract.

The Board, in proposing the $500,000 threshold, did so with the intent of exempting those companies which do not receive contracts in excess of $500,000 from the Government. However, it was decided in the interest of consistency in cost accounting practices that once a contractor had received a covered contract of that size, compliance with CASB rules, regulations and standards on contracts at the level established in Pub. L. 91-379 was appropriate. This is also consistent with the desire expressed by contractors to follow a single set of accounting practices. Further, the requirement for coverage of contracts in excess of $100,000 where the contractor already has received a covered contract in excess of $500,000 will permit the small contracts to be available for equitable adjustment if subsequently issued standards should become applicable. Moreover, once the administrative effort has been expended to comply with standards for contracts in excess of $500,000, compliance with standards on contracts above the statutory threshold of $100,000 requires little added effort.

With respect to the commentators' statements concerning the difficulties, when making an award exceeding $100,000, of determining whether a contractor or subcontractor had in existence a prior award exceeding $500,000, the Board feels that an administrative requirement can be established for obtaining this information. A similar requirement now exists concerning the disclosure statement, whereby contractors are required to submit a disclosure statement, state that they have previously filed a disclosure statement, or submit a certificate of monetary exemption. The Board feels that a similar requirement can be set concerning the $500,000 level. The Board is not persuaded that this matter would create problems of sufficient significance to eliminate coverage down to the $100,000 level.

In considering the advantages of the exemption as proposed compared to its assessment of the administrative difficulties foreseen by commentators, the Board is persuaded that its proposal relative to coverage of awards in excess of $100,000 should not be changed.

Exemption based on sales. A number of commentators urged that the Board establish an exemption based on sales, using either minimum annual dollar amount of sales to the Government, or Government sales as a percentage of total annual sales, or a combination of these two factors. The most frequently suggested amount was $10 million of sales to the Government or Government sales amounting to 10 percent of total annual sales. The objective sought by these commentators was an exemption of those companies or business units whose sales to the Government constituted a reasonably small portion of their total annual sales and whose business was essentially commercially oriented.

The Board has given lengthy consideration to the use of a sales basis for the establishment of a minimum threshold for compliance with its rules, regulations and standards. It did not use that basis at this time due to the nature of the problems involved in administering an exemption based on sales. In either of the situations suggested by commentators, the representation concerning the amount of sales must be made by the contractor and subsequently verified by the Government. This verification would impose very substantial and time-consuming efforts on both the Government and the contractor. Particularly in the case of Government sales as a percentage of total sales, Government representatives would be placed in the position of examining a contractor's total sales, including those made in its commercial business. Examination of a company's records concerning its total sales is not presently performed by Government procurement activities and would present new and unique problems to both parties as well as requiring substantial additional effort on the part of Government representatives.

An exemption based on sales would require a measurement period during which a contractor's status with respect to compliance with standards would be determined. Contracts under which sales were recorded during this period would not be subject to standards. If the volume of sales during the measurement period exceeded a stated threshold, a contractor would then be required to comply with standards under contracts received in subsequent periods. Thus, the contracts that brought the contractor under the Board's rules would not be subject to standards, while those received at a later time would be.

The Board has decided that the administrative problems involved with an exemption based on sales should be considered before establishing such a threshold. The Board will continue to study these problems and investigate whether exemptions based on criteria other than a minimum contract amount would be appropriate and consistent with the purposes of Pub. L. 91-379.

Retroactivity. Several commentators requested that the Board modify its proposal so as to provide retroactive exemption to existing contracts where the circumstances are such that these existing contracts would have been exempt if awarded after the effective date of the proposed regulation.

The Board has no authority to modify existing contractual agreements between the government procurement agencies and their contractors. However, the Board sees nothing inconsistent with its regulations or with Pub. L. 91-379 in modification by the procurement agencies of contracts in this category, assuming of course that the Government receives adequate consideration for deletion of the CAS requirements.

Increase minimum amount. A number of commentators recommended that the exemption proposed be increased to an amount greater than $500,000, the figure of $1,000,000 being frequently mentioned. The Board is not now prepared to raise further the minimum contract amount requiring compliance with its promulgations. The Board, in studying an exemption based on minimum contract amount, concluded that the $500,000 threshold was the most appropriate one for achieving its objectives, all factors considered. The Board will continue to examine various limitations but considers that the threshold established in the proposed exemption best meets its requirements and obligations at this time.

Effect of final payment under contracts subject to CAS clause. Several commentators urged that the exemption of contracts of $500,000 or less should not be dependent on the final payment on contracts which are subject to Board requirements, on the grounds that final payment can occur a substantial period of time after completion of work on a contract and that there are many technicalities in closing out a contract which do not involve cost accounting applications.

The Board considers this point to be well taken and has changed the requirement in § 331.30(b)(8) where it first appears to "notification of final acceptance of all items or work to be delivered." At that time it is considered that all direct costs will have been charged to the contract since all work will have been completed, and any further accounting transactions would be the result of adjustments not directly related to contract performance.

Reduction of contract price by exclusion of commercial items. Some commentators, in reading the introductory comments to the Board's initial publication of this exemption, interpreted the phrase "minimum contract amount requiring compliance" in a manner not at all intended by the Board. These commentators interpreted this phrase to permit the price of a contract subject to standards to be reduced by the value of those individual contract items or subassemblies of final contract items whose prices could be considered to be "catalog" or "market" prices, if sold separately. They requested that the regulation be clarified to reflect their interpretation of the Board's introductory comments.

Those requesting this clarification misunderstood the Board's intentions. The Board does not intend that the price of a contract be adjusted to exclude the price of items or subassemblies which, if purchased separately, might be exempt from the Board's promulgations. Consequently, the change in the regulation requested by commentators on this point would be completely inappropriate.

Definition of contractor. One commentator noted that the prefatory comments to the Board's September 27, 1974, publication specifically mentioned the fact that receipt of a contract in excess of $500,000 by one business unit of a multi-unit company would not in itself require other units of the same company to follow Board requirements. This commentator requested that the definitions of "defense contractor" and "defense subcontractor" contained in § 331.20 (b) and (c) be modified to reflect this intention by the Board.

As the Board stated in its September 27 publication, its contract requirements have been applied to business units, such as a profit center, division, subsidiary, or similar unit of a company, which perform the contract, even in those cases where the contract was entered into on behalf of the overall company rather than the business unit. This application of the Board's requirements to a performing business unit is well established and unchallenged, and clarification of the definitions of "contractor" and "subcontractor" does not appear necessary.

Effective date. Several commentators raised questions concerning the effective date of the eligibility for this exemption in relation to awards received prior to January 1, 1975. Contractors who have received a prime contract or subcontract in excess of $500,000 subject to cost accounting standards prior to January 1, 1975, and on which notification of final acceptance of all items or work to be delivered on that contract or subcontract has not been received, is a contractor who has "already received a contract or subcontract in excess of $500,000," as that phrase is used in § 331.30(b)(8). Therefore, today's publication requires that a contractor meeting this test will be required to comply with standards on all covered prime contracts or subcontracts in excess of $100,000 received after January 1, 1975, under the provisions of § 331.30.

PREAMBLE G

Preamble to Amendments of 2-2-76

This amendment added paragraph (b)(9) to § 331.30 and was published on February 2, 1976, at 41 FR 4809.

• Purpose. The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. This modification will provide a conditional exemption for contracts and subcontracts made with United Kingdom firms for performance substantially in the United Kingdom. •

The Cost Accounting Standards Board is authorized by Pub. L. 91-379 to prescribe rules and regulations exempting from its requirements such classes or categories of defense contractors or subcontractors under contracts negotiated in connection with national defense procurements as it determines, on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to be achieved by the Act. Pursuant to this authorization the Board has issued a regulation, § 331.30, *Applicability, exemption and waiver,* of Title 4, Code of Federal Regulations, which, among other things, establishes a procedure by which procuring agencies may request a waiver of the Board's requirements for a particular contract or subcontract.

The Board from 1972 to date has granted 45 waivers requested by procuring departments and agencies. Of that number, 23 were for contracts or subcontracts to be performed by United Kingdom firms each of which is a defense supplier to the U.K. Government and also is essentially a sole source supplier for the particular item being purchased by the U.S. Department of Defense. The waivers granted to U.K. firms have been based in general on the urgency and essentiality of the procurements, which were reported to preclude any alternative to making the proposed awards. However, the U.K. firms were reported as having objections to complying with the Board's rules and regulations, on the grounds that their accounting practices have been approved by the U.K. Government, their major customer, and may not thereafter be changed without further approval. They were reported as stating that they cannot assume an obligation to comply with Cost Accounting Standards which could be in conflict with U.K. Government Accounting Conventions and the governmentally approved accounting practices for the individual firms.

In view of the recurrence of this position and the high proportion of waiver requests involving U.K. firms, the Board undertook discussions with the U.K. Ministry of Defence concerning the application of Cost Accounting Standards and the Board's rules and regulations to firms which are U.K. defense contractors. As a result of these discussions it has been determined that U.K. defense contractors do disclose their accounting practices to the Ministry of Defence and that the Ministry of Defence approves companies' practices which then cannot be changed without further approval. It has further been determined that a Review Board for Government Contracts, whose chairman and members are nominated by the Government and industry and appointed by the Treasury, but which is established as an independent organization, among other duties periodically reviews and makes recommendations for changes in U.K. Government Accounting Conventions. The Review Board has also issued or sponsored certain cost accounting standards for use by U.K. firms in contracting with the Ministry of Defence.

On November 17, 1975, the Board published for public comment in the FEDERAL REGISTER (40 FR 53271) a proposal for a conditional exemption for U.K. firms performing substantially in the U.K. Nine responses were received to that publication. Responses were received from government departments, defense contractors, an industry association and two individuals. All of these comments have been considered by the Board, and the Board takes this opportunity to express its appreciation for the helpful suggestions which have been furnished.

The comments below summarize the major issues discussed by respondents to the initial publication and explain the Board's disposition of these issues.

U.K. Government Accounting Conventions. Two United States Government departments were concerned that the reference in the proposed conditional exemption to the obligation of U.K. firms to disclose cost accounting practices which would be in accord with U.K. Government Accounting Conventions implied or could be understood to require that when matters mandated by the Conventions were in conflict with certain requirements of the Armed Services Procurement Regulation and Energy Research and Development Administration procurement regulations, the policies of the Conventions would prevail.

One of the departments pointed out that the Conventions permit reimbursement of four kinds of costs which are either by U.S. law or by U.S. procurement policy not allowable costs in U.S. contracts. These are entertainment expenses, product advertising, certain donations and certain non-incurred capital costs. The Board recognizes that the Conventions deal broadly with matters which can be regarded as relating to both allocability and allowability of costs. They do indicate that in certain circumstances, the indicated costs are allowable costs under U.K. contracts. However, cost accounting practices covered by Disclosure Statements do not deal with the allowability of costs, only with their measurement and allocation. Where appropriate, a disclosed practice must result in measurement and allocation of a cost in accord with the Conventions; whether that cost is or is not allowed as a cost under U.S. contracts is a matter for agreement by the parties to the contract and is not affected by the requirement that disclosed cost accounting practices be in accord with the Conventions.

Secondly, the department points out that the profit formula used by the U.K. Government is different from the profit formula used in U.S. negotiated procurements. The U.K. profit formula, however, is not a part of the U.K. Government Accounting Conventions governing cost accounting practices, nor does the Disclosure Statement deal with policy on which profits are determined. Consequently, a requirement that disclosed cost accounting practices be in accord with the Conventions does not impinge on the authority of U.S. officials to prescribe policy for the determination of profits under U.S. prime or subcontracts.

Thirdly, the department notes that there are differences between the U.K. Government Accounting Conventions concerning independent research and development and the provisions in ASPR Section XV which are used for compliance with Pub. L. 91-441. Pub.

L. 91-441 makes Department of Defense appropriations unavailable for payment of a contractor's independent research and development or bid and proposal costs, unless the work which is paid for has a potential relationship to a military function or operation and unless other conditions are met. The most important of the other conditions is that there be an advance agreement with the contractor. What has been said above about the allowability of costs is applicable to this point also. Furthermore, nothing in the Board's conditional exemption in any way controls the terms and conditions upon which the Department of Defense may agree in advance with a U.K. firm for the reimbursement to it of independent research and development and bid and proposal costs.

Additionally, the department notes potential differences in the treatment of depreciation costs under the Conventions and under the applicable ASPR requirements, unmodified by the Board's Cost Accounting Standards. The comment does not specify, nor does the Board find, any significant differences at present. The Board does recognize that both the U.S. and U.K. Governments may modify their tax laws and their procurement regulations with an objective to encourage capital investment, and that differences could some day arise. In such case, the Conventions permit sufficient flexibility in individual cases to allow U.S. agencies to reach agreement with U.K. firms on appropriate annual depreciation costs.

Finally, this department has consistently requested unqualified waivers from the Board for use in its prime and subcontracts with U.K. firms. Such firms have in fact been required to follow U.K. Government Accounting Conventions on their work for the U.K. Government, and the department has been able to negotiate mutually agreeable prices for contracts with them despite this circumstance. Under the Board's conditional waiver, the department will have the advantage of a Disclosure Statement from such firms, which could not have been available when an unconditional waiver was sought and which should be of material assistance in the negotiation and audit of new contracts.

The Board is glad that these questions were raised but does not believe it is necessary to modify its proposed conditional exemption to resolve them.

It is appropriate to note here that the Board has not specifically required access to records of U.K. firms by appropriate U.S. officials, as it might have done. Such a requirement appears unnecessary in view of the standard provisions for access to records contained in U.S. defense contracts and subcontracts for performance in the U.K. Access to records through such standard provisions in those contracts will be adequate to assure contractor compliance with the consistency requirement of the conditional exemption.

Another commentator opposed the proposal largely on the basis of his belief that the proposal would require adoption by U.S. price negotiators and auditors of the pricing practices followed by the U.K. Ministry of Defence. This belief appears to have been based on the reference in the proposal to U.K. Government Accounting Conventions. The Board sees nothing in the conditional exemption which would require U.S. negotiators to accept pricing practices contrary to U.S. procurement regulations and the agreements which U.S. negotiators reach with U.K. firms in the pricing of prime or subcontracts.

This commentator also indicated that not all U.K. firms which are U.S. prime or subcontractors are also suppliers to the U.K. Government. The Board agrees that this could be the case and believes that if so, it is not appropriate for the Board to require that all U.K. firms necessarily adopt the U.K. Government Accounting Conventions. It has consequently modified its proposal to provide that disclosed practices must be in accord with the Conventions only when the disclosing contractor is already required to follow the Conventions. Thus, certain U.K. firms may be subject to neither Cost Accounting Standards nor U.K. Government Accounting Conventions. In such cases, U.S. negotiators must use that firm's Disclosure

Statement in arriving at agreement on the cost accounting practices to be followed in contracts subject to the conditional exemption.

Retention of disclosure statements. A commentator pointed out that while the Board had proposed that Disclosure Statements submitted by U.K. firms be filed with the U.K. Ministry of Defence, the Board had not specified that the Statements would be retained in the Ministry. Since that was in fact the Board's intention, the Board has adopted a modification to its proposal in order to make that intention clear.

Prime contractor-subcontractor relationships. Two matters relating to prime contractor-subcontractor relationships were raised. A commentator pointed out that a U.K. subcontract might be subject to price adjustment if the subcontractor changed its disclosed cost accounting practices during contract performance. In such a case, the Government's action would presumably be to require a corresponding change in the cost or price of the prime contract. The Board agrees that this is so, and prime contractors may wish in the future, as some have done in the past, to obtain agreement with U.K. subcontractors for appropriate indemnification in the event the subcontractor's change in practices causes a modification in the cost or price of the prime contract. The Board previously discussed this situation in its original publication of 4 CFR 331.50 and does not consider that specific language addressed to this matter is required to be included in the conditional exemption.

Another commentator stated that it was confident that the Board did not intend that the conditional exemption apply to U.S. subcontractors under prime contracts with U.K. firms and urged the Board to address this matter specifically. The Board's proposal does not require any flow-down of the clause, "Consistency in Cost Accounting Practices", from U.K. prime contractors to first tier or lower tier subcontractors. The Board may, after experience in use of that clause is gained, reconsider this matter. In that case, the Board would then have to consider whether it would be appropriate for the Board to require that a U.K. prime contractor be required to pass down to any subcontractor, whether or not a U.S. subcontractor, a more extensive contractual obligation than is imposed on the prime contractor. For the time being, the Board notes the likelihood that U.S. subcontractors under U.K. prime contracts will already be subject to Cost Accounting Standards by reason of other covered prime or subcontracts which that firm has entered into. If this prior coverage has not taken place, the Board believes that the value of achieving coverage through a flowdown provision in a U.K. prime contract is too insignificant to justify the administrative complexities of such a provision.

Further exemptions for foreign suppliers. A commentator, not wishing to comment on the present proposal, nevertheless recommended that the Board exempt all foreign suppliers, on the ground that problems in the administration of the CAS clause are matters of contention and, in the opinion of the commentator, pose relatively greater difficulties in the administration of foreign contracts.

The Board has announced the establishment of projects to investigate the administrative concerns of this commentator and others, and if those concerns prove to be substantial, the Board will take appropriate action. In the more than four years during which the CAS clause has been required to be included in all appropriate foreign contracts and subcontracts, absent a waiver, the Board has heard of no problem in the administration of the clause which has posed any problem in foreign contracts.

Whenever the Board believes a waiver of the CAS clause for foreign firms has been persuasively proposed by a contracting agency, it will grant such a waiver, but the Board's experience to date does not indicate to it any reason to consider a blanket waiver for all foreign prime contracts and subcontracts.

Miscellaneous comments. One commentator, from a major defense contractor, deserves note by the Board because of what the Board perceives to be major misconceptions and erroneous assumptions underlying the comment.

The comment opposed the proposal for a conditional exemption and favors an unqualified exemption. One reason given, to quote from this comment, is:

> By requiring a contract clause which will provide for a penalty to be paid by the U.S. prime contractor in the event that a U.K. subcontractor fails to consistently follow disclosed cost accounting practices where such failure results in increased costs paid by the U.S. Government, is to impose on the U.S. primes an obligation so vague and impracticable as literally to be unique in the history of bilateral contracting.

The Board believes this comment is wholly inaccurate. First, the obligation to consistently follow disclosed or established cost accounting practices is not imposed by the Board's current proposal—it has been present in every U.K. prime contract or subcontract subject to the CAS clause. Secondly, exactly the same obligation of a prime contractor has existed for years with respect to every subcontract it makes which includes the CAS clause. The Board does not believe that the obligation arising under the conditional exemption is either vague or impracticable, and it knows it is not unique.

Additionally, this commentator with respect to the same obligation stated:

> For the U.S. Government to impose such alien rules on the defense contracting community in the United Kingdom * * * where neither the Government of the United Kingdom nor the contractors have determined for themselves that there are benefits to the imposition of such punitive rules regarding accounting practices seems patently absurd. Further, to impose on the procurement process such a nebulous and one-sided contractual requirement by the use of the regulatory procedures which will render the clause "mandatory and non-negotiable" is to express an unwarranted contempt by the United States for the standards and practices of business accounting and contracting procedures of the United Kingdom.

Apart from the commentator's several adverse characterizations of the Board's requirements, which are discussed generally below, this portion of its comment does not appear to recognize that the Board's proposal was discussed with the U.K. Government and with representatives of the British defense industries. Through meetings in both Washington and London and through continuing, close consultations, the Board has confidence that its proposal has been carefully reviewed and discussed within the United Kingdom and that its adoption will be welcomed by the firms and governmental agencies affected by it. This careful consultation, and the Board's subsequent proposal for a conditional exemption, arose out of the Board's respect for, not its contempt of, the standards and practices of cost accounting in the United Kingdom.

Finally, this commentator expressed its view that there have been no discernible benefits whatever from the Board's regulations and its further view that the Board has abundant evidence that its regulations requiring consistency in following disclosed cost accounting practices have resulted in "substantial impairment of the economy, efficiency, and effectiveness of procurement * * *". The commentator concluded this point by stating that since it regards the Board's consistency requirement to be "unfair, unworkable and doubtfully enforceable", it would use the proposed conditional exemption for U.K. firms only "with shame and reluctance."

The Board has received reports from procurement agencies of major benefits stemming from use of its consistency requirements, and the Board believes that they have unquestionably improved the economy, efficiency and effectiveness of procurement. The Board believes that those requirements are fair, workable and enforceable.

As noted above, the Board is currently investigating suggestions made by some U.S. defense contractors, including this commentator, to determine whether there are substantial problems in the administration of its requirements to follow disclosed accounting practices consistently. The commentator offers no information concerning any such problem, only its conclusion that the Board has acted wholly improperly in proposing the U.K. conditional exemption. The Board does not agree.

Costs and benefits. The Board discerns no significant cost or inflationary impact of the conditional exemption.

The benefits include a substantial reduction in the number of waiver requests for United Kingdom firms, while establishing a consistency requirement for all U.K. contractors which is necessarily lost when all Board requirements are waived.

A United Kingdom firm could find that its obligations to follow U.K. Government Accounting Conventions might require the firm to change a disclosed cost accounting practice. In such an event, the Board hopes that the cost impact on U.S. contracts or subcontracts of any such change would be negotiated in advance of the effective date of a change to the Convention, so as to avoid the imposition of any interest charges on increased cost paid by the United States. The negotiation relating to a change in disclosed practices would be patterned on the similar negotiation required under Section (a)(4)(B) of the Cost Accounting Standards Clause.

In view of the foregoing, the following change to Part 331 of the Board's regulations is being made effective February 2, 1976.

PREAMBLE H

Preamble to Amendments of 9-12-77

The amendments to 4 CFR Part 331, 42 FR 45625, Sept. 12, 1977 were published as a part of the document which set forth the original 4 CFR Part 332 and amendments to Parts 351 and 403. The complete Preamble appears in the supplement to Part 332.

SMALL BUSINESS

Several commentators urged that all businesses which qualify as small business concerns under the rules and regulations of the Small Business Administration be exempted. The February 16, 1977 proposal would have provided such an exemption only for a small business which received less than $10 million in awards during its preceding fiscal year. Modified coverage would have been provided for other small businesses. Research indicates that there are very few companies which would fall into the category of small businesses receiving awards of $10 million or more. In the interest of using a single test, i.e., whether the contractor qualifies as a small business concern, rather than a dual test which would result only in a few small businesses being subject to modified coverage, the Board has adopted the recommendation to exempt all small business concerns. Research indicates that if this action had been applied to Federal Fiscal Year 1976 it would have resulted in exemption of 196 small business concerns which were doing business with the Department of Defense and which had $460 million of contracts of the type subject to Cost Accounting Standards. Consequently, on average, each small business concern would have a relatively small amount of covered contracts.

OTHER CATEGORIES

Various commentators renewed previous recommendations that the Board exempt other categories of contracts and contractors. The categories included colleges, universities, nonprofit organizations, hospitals, and government-owned contractor-operated facilities. The Board has considered these recommendations and concluded that none of these categories should be exempted.

EFFECTIVE DATE

The effective date of the regulations being published today is March 10, 1978. Pub. L. 92-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

PREAMBLE I

Preamble to Amendments of 10-5-77

This document added § 331.71 and was published Oct. 5, 1977, at 42 FR 54254.

Summary. This modification of the Cost Accounting Standards Board's rules and regulations provides criteria for determining the materiality of costs in given circumstances, in applying words or phrases of materiality used in Cost Accounting Standards, and to limit price adjustments to material amounts of cost.

Supplementary information. A discussion of the background and public comments reveived in response to the initial publication of these regulations and of the principal issues considered in preparing the final promulgation precedes the regulations.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. The modification will provide criteria for determining the materiality of amounts of cost in given circumstances. The Board initially considered publishing a definition of the terms "cost accounting practice" and "change to either a disclosed cost accounting practice or an established cost accounting practice" along with the modification dealing with materiality. That definition is being handled separately by the Board, however, and will be considered at a later date.

The Board is authorized by Pub. L. 91-379 to prescribe rules and regulations for implementing Cost Accounting Standards. Pursuant to this authority, the Board is today issuing a modification to its regulations. Contractors and procurement agencies engaged in the implementation and administration of CASB rules, regulations, and Standards have recommended that the Board provide guidance concerning materiality in the administration of the Board's rules, regulations, and Standards.

Representatives from various organizations affected by Standards have pointed out that guidance in this area will facilitate the implementation and administration of CASB pronouncements. A similar recommendation was also received by the Board at an Evaluation Conference in June 1975. The General Accounting Office's Status Report on the Cost Accounting Standards Program—Accomplishments and Problems (PSAD—76-154, Aug. 20, 1976), also referred to the need for guidance on this subject.

Research in this area included a review of data submitted by participants in the Evaluation Conference, an analysis of papers submitted by various contractors, professional groups, trade associations, and Government agencies, as well as a review of existing procurement regulations, and existing CASB promulgations. A Staff draft of an amendment dealing with materiality criteria and price adjustments was distributed on August 13, 1976. Responses from 53 sources contributed to the Board's further consideration of the issues involved in this proposed amendment.

A proposed amendment to the Board's regulations was published in the FEDERAL REGISTER on February 3, 1977 (42 FR 6591). A total of 45 responses were received from individual companies, Government agencies, professional associations, industry associations, universities, and others. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by the organizations and individuals have resulted in a number of changes in the amendment being promulgated today. The following material summarizes the issues regarding materiality that were discussed by respondents in connection with the proposed modification and explains the changes made to the proposal published February 3, 1977. The still relevant portions of the comments which accompanied the February 3, 1977, publication have been incorporated in this material.

MATERIALITY CRITERIA

Generally, commentators felt the proposed materiality criteria were a necessary, positive and useful step. However, some commentators suggested that the proposed criteria were not sufficiently specific and would not resolve the materiality questions that currently exist. Some commentators suggested that quantitative criteria be added to the proposed regulation; others suggested that the criteria proposed were suitable.

At the present time, the Board is of the opinion that quantitative limits should not be established for materiality determinations. The essence of materiality criteria is to allow for the excise of judgment; and absolute dollar amount in one case may be material while in another case the same amount may be immaterial. Accordingly, quantitative limits have not been added to the proposed amendment.

The materiality criteria being promulgated are designed for use in a variety of situations and to resolve issues which have been raised by various sources. Cost Accounting Standards establish the cost accounting appropriate for the determination of contract costs. Departure from the requirements of these Standards may occur and the cost effects of such departure may be immaterial. The criteria serve to limit price adjustments to material amounts of cost. The regulation also describes the actions to be taken when immaterial amounts of cost are involved in noncompliance with Standards. The criteria for materiality are also to be used in applying words or phrases of materiality used in Cost Accounting Standards. In particular Standards, the Board will continue to give consideration to defining materiality in a specific manner as to either the entire Standard or any provision thereof, whenever it appears feasible and desirable to do so.

ADMINISTRATIVE COSTS

Commentators proposed that the administrative cost of processing a change in cost accounting practice to both the Government and the contractor should be one of the criteria used in determining materiality. The Board's initial publication did not provide for consideration of these costs in determining materiality. Generally, such costs on the part of both the Government and the contractor are absorbed as part of their routine operations. On a conceptual basis, the determination of materiality should be made considering only the amount of costs affected by the proposed changes. As a practical matter, however, the administrative cost to process a contract price adjustment is a factor in a materiality decision.

The Board is persuaded that the administrative cost of processing a change in cost accounting practice should influence a decision as to materiality. For example, if it is estimated that costs would be changed by $10,000 through processing a change at a Government-contractor administrative cost of $10,000, then processing the change would be nonproductive whether or not, considering all materiality factors, the estimated change in costs of $10,000 would be judged material. Accordingly, the Board has added a provision to this modification dealing with such costs.

MEASUREMENT OF COST IMPACT

Commentators suggested that the Board's regulations provide that initially the determination of materiality should be done on a gross, overall, basis rather than on an in-depth cost impact study. These commentators asserted that a provision of this type would help to reduce the time and cost of evaluating and processing proposed changes which are judged to have an immaterial impact. Procedures for measuring and processing cost impact due to both changes in cost accounting practice and noncompliances with Cost Accounting Standards have been developed by the procurement agencies, and they now require an estimate of the general dollar magnitude of the change as a first step in the process. The Board encourages the use of the materiality criteria promulgated today in conjunction with the existing two-stage cost impact evaluation procedure provided in procurement agency regulations. The Board believes that the effective use of procedures established in agency regulations will accomplish the saving in time and cost desired.

Some Government commentators proposed that § 331.71(b)(2) be deleted. They expressed the view that it dealt with administrative matters and not criteria for the determination of materiality. The question of both the contractor's and the Government's responsibility in situations where noncompliance with Cost Accounting Standards resulted in a cost impact which is immaterial has frequently arisen. The Board believes that the implementation and administration of cost accounting rules, regulations, and Standards will be facilitated by a statement of the Board's position on this matter. Accordingly, the Board believes that the section in question should be retained in its regulations.

RETROACTIVE APPLICATION

Commentators expressed concern that § 331.71(b)(2) would be applied retroactively to immaterial items. The language of this section requires that it be applied to the accounting period for which the cost impact of a noncompliance becomes material and to succeeding cost accounting periods. In any cost accounting period prior to that, by reason of the provisions of this requirement, the cost impact of the noncompliance would have been determined to be immaterial. Thus, no contract modification was or is required.

ILLUSTRATIONS

The February 3, 1977, proposal contained two illustrations of the application of the materiality criteria. A number of commentators stated that the illustrations were too basic to be useful, and that the problems related to the determination of materiality are too numerous and too complex to be adequately illustrated in a regulation of this type. The commentators suggested that the illustrations be eliminated. The Board agrees, and has eliminated the examples in this section.

PREAMBLE J

Preamble to Amendments of 3-10-78

The document published at 43 FR 9775, Mar. 10, 1978, added § 331.20(h), (i), and (j), § 331.50(a)(4)(C), § 331.51, § 332.50(a)(5), and § 332.51, revised § 331.50(a)(4)(B), and (d) introductory text and (d) (1) and (2), and amended Parts 351, 403, 406, and 409.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to part 331, Contract Coverage, and part 332, Modified Contract Coverage, of its rules and regulations. The Board is also withdrawing a proposal to modify § 331.70. This modification being adopted will (1) provide definitions of the terms "cost accounting practice," and "change to either a disclosed cost accounting practice or an established cost accounting practice," (2) permit the negotiation of equitable adjustments to reflect the cost impact of changes agreed to by both parties to the contract, and (3) establish the effective date for application of standards to subcontracts. The December 1976 proposal to modify the method of determining increased costs is being withdrawn.

The Board is authorized by Pub. L. 91-379 to prescribe rules, regulations, and modifications for implementing cost accounting standards. Pursuant to this authority, the Board is today issuing modifications to its regulations. Contractors and procurement agencies engaged in the implementation and administration of CASB rules, regulations, and standards have recommended that the Board provide guidance concerning the meaning of "cost accounting practice" and "change to either a disclosed cost accounting practice or an established cost accounting practice."

Representatives from various organizations affected by standards have pointed out that guidance in these areas will reduce disagreement and facilitate the implementation and administration of CASB pronouncements. Similar recommendations were also received by the Board at evaluation conferences in June 1975 and October 1977. The General Accounting Office's Status Report on the Cost Accounting Standards Program—Accomplishments and Problems," (PSAD-76-154, August 20, 1976), also referred to the need for guidance on these subjects.

Research in this area included a review of data submitted by participants in the evaluation conferences, an analysis of papers submitted by various contractors, professional groups, trade associations, and Government agencies, as well as a review of existing procurement regulations, the Internal Revenue Code, Accounting Principles Board Opinion No. 20, and existing CASB promulgations. A staff draft of amendments containing definitions of "cost accounting practice" and "change to either a disclosed cost accounting practice or an established cost accounting practice" was distributed on August 13, 1976. Responses from 53 sources contributed to the Board's further consideration of the issues involved in these proposed amendments.

Proposed amendments to the Board's regulations were published in the FEDERAL REGISTER on February 3, 1977 (42 FR 6591). A total of 45 responses were received from individual companies, Government agencies, professional associations, industry associations, universities and others. The proposed amendments were revised and republished for comment on October 21, 1977 (42 FR 56130) and included a proposed change to the CAS contract clause. A total of 40 responses were received to that publication.

The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. These comments have resulted in a number of changes and improvements in the amendments being promulgated today. The following material summarizes the issues discussed by respondents in connection with the proposed modification and explains the changes made to the proposals published February 3 and October 21, 1977. The still relevant portions of the comments which accompanied the earlier publications have been incorporated in this material.

DEFINITION OF COST ACCOUNTING PRACTICE

The need for a definition of "cost accounting practice" has been raised by numerous inquiries from the field and by participants in the evaluation conferences. The Board agrees, and believes that a definition of this term can reduce disputes and contribute to increased uniformity in the administration of the CAS contract clause.

A number of commentators expressed the view that the proposed definition was workable and useful as presented, would serve to reduce disagreements, and would facilitate the administration of cost accounting standards. Some said that the proposal, if adopted, would go a long way towards solving several problems identified in earlier written communications to the Board and oral presentations to the Board and its staff. Some encouraged the Board to promulgate the rule at an early date and commended the Board for taking a very significant step towards solving one of the troublesome and difficult areas of Cost Accounting Standards.

Other commentators suggested that the proposed definition went beyond the authority of the Board in that it included both the measurement of cost and the assignment of cost to cost accounting periods.

They asserted that these are financial accounting topics and are not within the realm of cost accounting. Still other commentators stated that the Board was dealing with detailed practices and procedures rather than Cost Accounting Standards and principles.

As early as March 1973, in the "Statement of Operating Policies, Procedures, and Objectives" and more recently in the May 1977, "Restatement of Objectives, Policies and Concepts," the Board stated that Cost Accounting Standards will be established to define and measure cost, determine the cost accounting periods to which costs are assigned, and determine the manner in which costs are allocated to covered contracts. The Board has spoken directly to the measurement of cost in Cost Accounting Standards 404 and 412 and to the assignment of costs to cost accounting periods in Cost Accounting Standards 408, 409 and 412. The definitions being promulgated today are consistent with the Board's authority and previously adopted view that cost accounting practices include measurements of cost, assignment of cost to cost accounting periods and allocation of costs to cost objectives.

Questions have been raised as to whether the measurement of cost includes the determination of the price to be paid by the contractor for goods and services. From the beginning of the project to define a cost accounting practice, the Board has taken the position that the determination of the amount paid or a change in the amount paid for units of goods and services does not constitute a change in cost accounting practices. The definition has been revised to convey this concept more clearly.

With respect to commentators' views on the difference between Cost Accounting Standards, principles, and practices, the Board's 1973 "Statement of Operating Policies, Procedures, and Objectives" and the 1977 "Restatement" describe a Cost Accounting Standard as:

> A Cost Accounting Standard is a statement formally issued by the Cost Accounting Standards Board that: (1) Enunciates a principle or principles to be followed, (2) establishes practices to be applied, or (3) specifies criteria to be employed in selecting from alternative principles and practices in estimating, accumulating, and reporting costs of contracts subject to the rules of the Board. A Cost Accounting Standard may be stated in terms as general or specific as the Cost Accounting Standards Boards considers necessary to accomplish its purpose.

This position is similar to the approach the accounting profession takes in dealing with accounting principles for financial reporting. The Accounting Principles Board Opinion No. 20, Accounting Changes, states:

> The term accounting principle includes not only accounting principles and practices, but also the method of applying them.

Thus, in line with previous statements, the Cost Accounting Standards Board reiterates its position that the terms "principles and practices" include methods and techniques. The Board's position is consistent with Pub. L. 91-379 and reflects one of the principal purposes of setting Standards, which is to measure the full cost of supplies and services acquired by the Government in a way that is fair to both buyer and seller.

Commentators also raised the question of what should be the required level of detail of a cost accounting practice. The issue is what is the appropriate and necessary level of accounting detail for effective implementation of Pub. L. 91-379. For cost allocation purposes the Board has concluded that the level of detail should include not only the type of base, e.g., direct labor, but also the composition of that base, e.g., the elements of labor costs comprising the base. Similarly, the level of detail should include the types of indirect cost pools as well as the components or items of cost which make up those pools. As to measurement of cost, the level of detail includes identification of components of a particular item of cost and the basis on which cost is measured.

DEFINITION OF CHANGE TO EITHER A DISCLOSED COST ACCOUNTING PRACTICE OR AN ESTABLISHED COST ACCOUNTING PRACTICE

With respect to the February 3, 1977, proposed definition, commentators requested expansion of those changes in cost accounting practices which would not be subject to the provisions of paragraphs (a)(4) and (a)(5) of the Cost Accounting Standards contract clause (4 CFR 331.50). Commentators recommended that changes to improve management controls, accounting changes which the Government and contractors believe would be beneficial in the long run, and changes due to changed business circumstances should be added to § 331.20 as actions which are not considered as a change in cost accounting practice for purposes of paragraphs (a)(4) and (a)(5) of the Cost Accounting Standards Contract Clause (4 CFR 331.50).

The Board notes that in a dynamic business environment it may be desirable to make changes of many types. These changes may include organizational changes, changes in the way work is performed, and changes in the product produced. There may be a variety of reasons for these changes, such as better managerial control, new technology, or changed business conditions.

These business changes by themselves are not changes in cost accounting practices. Such changes may, however, cause a change in a contractor's cost accounting practices. In a circumstance where there is a change in a cost accounting practice, the contractor and Government must take certain action under the provisions of the CAS contract clause. Only when the contracting officer does not make the required determination under the new § 331.50(a)(4)(C) would contracts be amended to insure that the Government does not pay any increased cost as a consequence of the change.

The decision as to whether there is a change in cost accounting practice is made through an analysis of the circumstances of each individual situation based on the criteria being promulgated in these regulations.

It is to be expected that the accounting system must change—betterments, improvements, modifications or alterations to the system are necessary to accommodate the business changes discussed above. The Board notes that Pub. L. 91-379, in its provisions relative to failure of a contractor to follow consistently his disclosed practices, makes no distinction among the causes of changes in cost accounting practices. Thus, accounting changes of the types described by the commentators, which result in a failure of a contractor to follow consistently his previously disclosed or established practices, remain subject to the CAS contract clause (4 CFR 331.50). While a number of the suggestions made have been adopted and are discussed in the following material, the suggestions that changes in cost accounting practice due to changed circumstances or to improve management control be excluded from adjustment under the CAS contract cause have not been adopted by the Board. These types of changes are subject to review and agreement by the contracting officer and the contracts may be adjusted under new § 331.50(a)(4)(C).

A number of commentators urged that changes resulting from issuances of the Financial Accounting Standards Board should also be excluded from paragraphs (a)(4) and (a)(5) adjustments. The legislative history leading to creation of the Cost Accounting Standards Board shows that standards and principles issued for financial accounting purposes were not deemed suitable for cost accounting for negotiated Government contracts. The Cost Accounting Standards Board views its own work as relating directly to the preparation, use and review of cost accounting data in the negotiation, administration and settlement of negotiated defense contracts. The Board is the only body established by law with the specific responsibility to promulgate Cost Accounting Standards and these Standards have the force and effect of law in the negotiation, administration and settlement of defense contracts.

The Board seeks to avoid conflict and disagreement with similar organizations having other responsibilities in the area of accounting Standards and through continuous liaison makes every reasonable effort to do so. The Board will give careful consideration to the pronouncements affecting financial reporting and in the formulation of Cost Accounting Standards it will take these pronouncements into account to the extent it can do so in accomplishing its objectives. Nevertheless, the nature of the Board's statutory authority and its mission to establish Cost Accounting Standards for negotiated defense contracts is such that it must retain and exercise full respnsibility for meeting its objectives. Accordingly, the Board has not adopted this suggestion.

ALTERATIONS NOT CONSIDERED CHANGES IN COST ACCOUNTING PRACTICES

The February 1977 proposed definitions specifically provided that certain contractor actions should not be considered as changes in cost accounting practices. These include the initial adoption of a cost accounting practice or the elimination of a cost accounting practice. A number of commentators expresssed the opinion that the accounting treatment of a cost which up to a given point in time has been immaterial in amount and now becomes material in amount is a situation very similar to the establishment of a practice for the initial incurrence of a cost. They pointed out that Accounting Principles Board Opinion No. 20, Accounting Changes, treats this situation as a first time incurrence of a cost rather than a change in accounting principle or practice.

The Board has previously expressed the position that administration of Cost Accounting Standards should be reasonable and not seek to deal with immaterial amounts of costs. In concert with this position, the Board in the October 1977 proposal modified § 331.20(i) to provide that a change in accounting for a cost which has previously been immaterial and now becomes material is not a change in cost accounting practice.

The alterations described above are not treated under the CAS contract clause as changes in cost accounting practices. They can, however, result in the establishment of cost accounting practices. Where such is the case, the requirements of the CAS contract clause (4 CFR 331.50) will apply. The new practices must be followed consistently on all CAS contracts, and Disclosure Statements updated where appropriate.

SUBSEQUENT CHANGES UNDER A STANDARD

The Board's October 1977 proposal provided that when a Standard with which the contractor has complied subsequently requires the contractor to alter a cost accounting practice in order to remain in compliance, that alteration shall not be a change in cost accounting practice for purposes of paragraphs (a)(4) and (a)(5) of the CAS clause. Some commentators said that theis proposal was inconsistent with the Board's position in 4 CFR Part 403. Others said that unless a contract adjustment can be made under CAS regulations no acceptable adjustment mechanism was available. Most commentators generally felt that changes of this type should be dealt with under CAS regulations.

The Board believes that this provision is not inconsistent with 4 CFR Part 403. In that Standard, the Board was limiting use of equitable adjustment to the first time that a particular allocation provision of the Standard was applied.

The Board recognizes the points made by the commentators, however, and has concluded that a change in cost accounting practice to remain in compliance with a Standard does not constitute a failure to comply with Cost Accounting Standards or to follow consistently disclosed cost accounting practices. Accordingly, the Board has deleted from the regulations being published today the provision excepting adjustments for subsequent changes under a Standard from being considered under paragraph (a)(4) of the Board's regulations, because changes of this type will be covered by new paragraph (a)(4)C) of the CAS contract clause which calls for negotiation of an equitable adjustment. The Board also notes that contractors who have filed Disclosure Statements would be required tc amend such Statements to describe the practices to be followed.

CHANGE COMPELLED BY LAW OR REGULATION

A number of commentators urged the Board to delete the exception in its October 1977 proposal for price adjustments under cost accounting standards for changes compelled by law or regulation § 331.20(i)(3). Some contended that all changes, regardless of motivation, should be considered for adjustment under the Board's new proposed subparagraph dealing with changes agreed to by the parties. Other commentators urged the Board to remove the exception to preclude a contractor from experiencing a windfall or suffering a loss because of such changes.

The Board agrees with the suggestions made to delete this paragraph, because the Board feels that all contractor proposed changes in cost accounting practice should be considered for contract adjustment. Therefore, a contractor desiring to make a change in cost accounting practice for any reason must negotiate with the contracting officer under the appropriate paragraph of the CAS contract clause.

Should a situation arise where major changes in cost accounting practices would be required by contractors to comply with express provisions of a law or regulation, the Board would seek to accommodate any such requirement by a change in its standards, rules or regulations.

The Board has deleted from these amendments the proposed § 331.20(i)(3) which dealt with changes compelled by law or regulation.

ILLUSTRATIONS

Many commentators said that all or some of the illustrations should be deleted, while other commentators said they should be retained. The Board included the illustrations to demonstrate the application of the definitions in situations of the type which have been reported to the Board in the past.

The Board noted that some of the illustrations dealing with changes in organization were being misinterpreted. In effect, the commentators expanded the illustrations to include situations not set forth in the illustrations. The Board concluded that in view of the extent of misinterpretation, it would be questionable value to revise the illustrations to cover all the situations described by commentators. Accordingly, several illustrations dealing with accounting changes related to organizational changes have been deleted.

As the Board stated when the proposed definitions were published in February 1977, the accounting effects of any organizational change must be considered separately and a final decision concerning a change must be based on an evaluation of those effects. Thus, an organizational change per se is not a change in cost accounting practice. One must look at any accounting revision brought about for any reason, including one caused by a change in organization.

By including the illustrations the Board does not intend to imply that all possible situations are covered nor are the illustrations to be used as limitations for accounting changes. The Board believes that the changes made to this section are responsive to the statements made by commentators.

CONTRACT CLAUSE

The Board proposed in October 1977 that where the parties agree to a change in cost accounting practice they should negotiate an equitable adjustment for any cost impact on existing contracts. Most commentators agree with this proposal but some felt that the contracting officer's agreement should not be necessary. Others urged the Board to state that a contracting officer's disagreement with a change is subject to the disputes clause of the contract. Further, a number of commentators suggested that the new contract adjustment paragraph be renumbered (a)(4)(C) to avoid confusion with the pre-existing numbering series. Finally, some commentators asked if the Board planned to make comparable revisions to its Part 332, Modified Contract Coverage.

The October 1977 proposal was in response to urging by both contractor and Government agency representatives to establish an alternative to paragraph (a)(4)(B) for adjusting contracts where both parties agreed that a change in cost accounting practice was desirable. Under that proposal, a method was established providing for equitable adjustment for these changes. The Board does not agree that contracting officer's agreement is not necessary and remains convinced that Government agreement to the change is essential to protect the Government's interests.

With respect to the treatment of a contracting officer's disagreement with a proposed change in cost accounting practice under the disputes clause of the contract, the Board believes this should be determined under agencies' general rules governing appeals from various types of decisions by contracting officers. Accordingly, the Board has not specifically provided for the application of the disputes clause in this situation.

The Board agrees with the suggestion concerning the renumbering of the paragraph dealing with equitable adjustments for changes in cost accounting practices agree to by the parties. The amendments being published today have that paragraph numbered (a)(4)(C). Designating the new paragraph as (a)(4)(C) eliminates the need to change citations in other subparagraphs in section 331 from those previously existing in CASB regulations.

With respect to the question concerning comparable revisions to Part 332, the new definitions and illustrations are incorporated in § 332.20 by the existing cross reference to § 331.20. The Board's regulation concerning changes in cost accounting practices agreed to by the contracting officer will be incorporated in §§ 332.50(a) and 332.51 by amendments being published today.

INCREASED COST PAID

Commentators at the 1977 Evaluation Conference and respondents to the February 3 and the October 21, 1977, proposals requested that the Board remove from its regulations the prohibition against increased costs paid because of changes in cost accounting practices (§ 331.50(a)(4)(B)) and/or that the expression "increased costs paid" (4 CFR 331.70) be redefined to exclude fixed price contracts. The Board has established a priorty project to perform a comprehensive review of Part 331 of its regulations, including the treatment of increased costs paid.

CONTACTING OFFICER DETERMINATION

Many commentators objected to the Board's including a requirement that a contracting officer make a finding that a change is desirable and is not detrimental to the interest of the Government. Some claimed that such a requirement encroached on management's prerogative to design an accounting system to meet its needs; others said the decision concerning changes was an administrative matter, better left to the agencies. Others suggested that different terms be substituted for some of the words. Finally, some commentators said that the Board should require only that agencies prescribe appropriate regulations for the use of the equitable adjustment provision for accounting changes agreed to by the parties.

The Board understands the concerns expressed by the commentators on this matter. It should be recognized, however, that the Board is proposing that equitable adjustments be negotiated for accounting changes not required by Standards. This type of provision was requested by many contractors and Government agencies in the past. These groups insist that agreed-to changes should be allowed and that the contractor should not be required to pay for any increased costs on existing contracts resulting from such desirable changes. The Board is responding to these requests by providing for equitable adjustments for those proposed changes with which the contracting officer agrees if he finds them to be desirable and not detrimental to the interests of the Government.

Management certainly can propose any changes it feels desirable for its own accounting system. If a change is not desirable from the Government's point of view, the Board sees no justification for permitting the contractor to realize economic benefits on existing contracts from the change.

The Board's regulation merely recognizes the contracting officer's position and does not encroach on the administrative responsibilities of the procurement agencies. A contracting officer would routinely make certain that a contractor's proposed change is not detrimental to the Government before agreeing to allow increases in contract prices.

Some suggested alternative words for "desirable" were: "Appropriate, warranted, equitable, fair or reasonable." The Board concludes that all of these tests are encompassed by the Board's language. Accordingly, this statement has not been changed.

The Board expects adminstrative agencies to publish regulations they feel necessary to define what they conclude is "desirable and is not detrimental to the interest of the Government." Thus, the Board does not agree that it is getting involved in administrative matters.

The Board agrees with the commentators who suggested that the second sentence of § 331.51, which required that the contracting officer document the basis for his finding, be eliminated. The Board believes that the stated documentation requirement is redundant with other language in this subparagraph, and accordingly, that sentence has been eliminated.

WITHDRAWAL OF PROPOSED ALTERNATIVE METHOD OF DETERMINING "INCREASED COSTS"

On December 29, 1976, a proposal was published in the FEDERAL REGISTER to amend § 331.70(b) which, if adopted, would have permitted procurement agencies to use either an estimate-to-complete approach or an original-negotiation-data approach to determine increased costs paid by the United States. As proposed, agencies would have been authorized to use the estimate-to-complete method when negotiations had not been based on cost estimates or such estimates were not readily determinable by the procuring agency.

Most of the comments received expressed opposition to all or part of the proposal. Upon reexamining the subject in light of the comments received, the Board concludes that the proposed alternative method would not provide sufficient improvement in the administration of Standards to warrant its adoption. Additionally, none of the alternatives suggested by the commentators appears likely to benefit the procurement process materially. Accordingly, the proposal to amend § 331.70(b), Contract Coverage, as published in the FEDERAL REGISTER of December 29, 1976, is hereby withdrawn. This subject will be considered in the Board's comprehensive review of Part 331.

COSTS AND BENEFITS

The definitions promulgated today fill a void that thad been recognized in numerous comments to the Board and the procurement agencies. The Board believes that the material being promulgated today is in keeping with its responsibility and authority as provided in Pub. L. 91-379. The Board believes further that the appropriate use of the definitions can significantly reduce the time and effort involved in the administration of Cost Accounting Standards. The Board concludes, therefore, that there will be virtually no costs involved in implementing these regulations and that there will be significant benefits with no inflationary effects.

MISCELLANEOUS AMENDMENTS

A number of miscellaneous amendments are being published today to conform language in certain paragraphs of Title 4 CFR Parts 351, 403, 406 and 409. These amendments add references to the new § 331.50(a)(4)(C).

EFFECTIVE DATE

The following changes to the Board's regulations are being made effective today, March 10, 1978.

PREAMBLE K

Preamble to Amendments of 6-8-78

The document published as 43 FR 24819, June 8, 1978, added § 331.30(b)(3) and revised §§ 403.70(b), 408.70, and 410.70 and 415.80. Portions of this preamble, relating to Parts 401 through 410 and 415 have been omitted: they can be found in the supplements to their respective parts.

The Cost Accounting Standards Board is authorized by Pub. L. 91-379 to prescribe rules and regulations exempting from its requirements such classes or categories of defense contractors or subcontractors under contracts negotiated in connection with national defense procurements as it determines on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to be achieved by the Act.

The Cost Accounting Standards Board has been requested by several Federal agencies and by representatives of educatioal institutions to consider the extent to which its standards, rules, and regulations should apply to educational institutions that are subject to Federal Management Circular 73-8 or OMB Circular A-21 and to consider whether an exemption for such institutions from Board promulgations is appropriate. The Board had provided exemptions for them in certain specific standards where the application would not be appropriate.

On March 15, 1978, the Board published for comment in the FEDERAL REGISTER (43 FR 10699) a proposal to exempt most educational institutions. The exemption would not apply to contracts with federally funded research and development centers operated by such educational institutions. Forty-seven comments have been received, all of which favored the proposed action by the Board although some respondents requested minor changes and clarifications.

A few commentators expressed concern that an educational institution receiving a contract from the Government could apportion the contract effort between the university and the FFRDC to take advantage of differences in cost accounting required under CAS and under FMC 73-8. If this becomes a problem, the procuring agencies are able to take the necessary corrective action.

Several commentators noted that there could be some misunderstanding concerning the applicability of CAS 403 to the university which is functioning as a "home office" for an FFRDC. The Board intends that CAS 403 not be applicable to the university in this situation and minor changes have been made to the language to clarify its intent.

One commentator indicated that the definition of FFRDC is not meaningful and suggested that the Board list the criteria by which NSF designates an FFRDC. Since coverage is intended only for those organizations designated as FFRDC's by the NSF based on whatever criteria they deemed appropriate, inclusion of their current criteria would not be useful. Accordingly, no changes have been made in the definition included in § 331.30(b)(3).

One commentator noted that the removal of current exemptions from CAS 403, 408, and 410 for FFRDC's will require a transitional period. It is considered that the provisions of §§ 403.70(a), 408.80, and 410.80 will furnish sufficient time for compliance by the FFRDC's with those standards. Section 403.70(a) provides that a contractor, if not exempt, shall be required to comply at the start of his first cost accounting period following receipt of the award of a negotiated national defense contract making the standard applicable. A contract awarded after August 1, 1978, will make the standard applicable to a FFRDC. Consequently, a FFRDC must comply with CAS 403 as of the start of its next cost accounting period after receipt of a contract after August 1. Standards 408 and 410 apply in the same way. It is recognized that all FFRDC's do not necessarily receive a new contract each year and that annual funding may be by means of an amendment to an existing contract. Applicability would be at the start of a cost accounting period after receipt of a new contract or after receipt of the annual extension of an existing contract.

The Board having found the exemption appropriate and consistent with purposes sought to be achieved by Pub. L. 91-379, is modifying its regulations as set forth below.

PREAMBLE L

Preamble to Amendments of 11-14-78

The document published on Nov. 14, 1978, at 43 FR 52693 revised § 331.30 (b)(5), (c)(1) and (c)(2).

The Cost Accounting Standards Board is today promulgating amendments to its regulations dealing with exemptions for contracts and subcontracts performed by foreign governments and foreign concerns. On July 31, 1978, the Cost Accounting Standards Board published a proposal under which contracts or subcontracts with foreign concerns could be exempted from certain individual standards if an authorized official of a relevant Federal agency determines that application of the standards to such contracts or subcontracts is inappropriate. The Board received 12 comments on the proposal.

One commentator opposed the proposal as unnecessary because the Board itself has authority to grant exemptions when such action is appropriate and asserted that delegation is undesirable because such decisions are too important to be delegated. The Board agrees that decisions concerning exemptions are important and has carefully considered the proposed action in the light of all comments and other available information. Based on that consideration the Board has concluded that it should grant a specific categoric exemption. Consequently no delegations are needed. Moreover because of the categoric exemption, the need to amend individual standards is obviated.

One government agency to whom delegation of authority was proposed noted that in implementing the delegation, one of the factors it would consider in determining whether the application of an individual standard is appropriate is the matter of sovereignty. Because of the action being taken today, there is no need to comment on the appropriate weight to be assigned to that factor.

Another commentator also discussed sovereignty and suggested that the United States has no legal right to impose the requirements of its laws and regulations on foreign contracts. To support this assertion, the commentator cited an official of the Department of Defense who attributed some of the difficulties in foreign procurements to the insistence upon contracts rather than general agreements. Whether a contract or some other instrument is used is something to be decided by other agencies of the government and not by the CASB. The Board has long recognized that its Standards are not applicable to noncontractual arrangements and agrees with the suggestion that if the procuring agencies used some noncontractual arrangement to transact business with foreign contractors, CAS would be inapplicable to the transaction. However, when the parties agree to use a negotiated national defense contract or subcontract as the vehicle for transacting business, the agreement must include the standards, rules, and regulations of the Board.

One commentator expressed the opinion that no substantial benefit would accrue to the United States under the limited exemption originally proposed but that a complete exemption from all Cost Accounting Standards Board requirements would be beneficial. Instead of the proposed exemption and delegation, that commentator recommended that all contracts and subcontracts with foreign firms and governments be exempt from all CAS requirements. The Board does not agree that a limited exemption would produce no significant benefits but that a complete exemption would. Significant benefits accrue to the United States Government from all standards, in part because each standard enhances the likelihood of achieving the goal of uniformity and consistency set forth in Pub. L. 91-379. The Board believes that by exempting foreign contracts from some standards there is a detriment rather than a benefit insofar as the public law itself is concerned. Nonetheless the Board has been advised that the requirement to apply some standards has become a significant impediment to efficient, successful contracting with foreign concerns and foreign governments.

The exemption being granted today will remove that impediment while continuing to provide protection through the application of CAS 401 and 402. In addition, foreign concerns will still be required to file Disclosure Statements.

The requirements of CAS 401 and 402 are fundamental to any sound cost accounting program. In the Board's view application of these standards is essential to provide some assurance that a contractor's cost accounting practices are sufficient to provide reliable information on which to base the negotiation, administration, and settlement of contracts. Similarly, the requirement for disclosure which is also being continued unchanged, serves to assure that necessary information about cost accounting practices is available to the Government.

Several commentators recommended that in addition to contracts with foreign contractors, the Board should exempt contracts with foreign governments. The Board has concluded that this recommendation has merit and the exemption being promulgated today has been amended accordingly. Because the exemption established in 1972 for the Canadian Commercial Corp., an agency of the Canadian Government, is included in today's exemption action, the 1972 exemption is being withdrawn.

One commentator suggested a need to define "foreign concerns" and another recommended that "performance" be defined. The term "foreign concern" has already been defined by the Board in § 331.30(c)(2).

As to what constitutes "performance," the Board believes that in general it encompasses the contractor's activity under the contract up to the point of inspection and acceptance of the items called for by the contract. However, because of the complexity and variety of contracts, the Board believes that the contracting agency can best determine whether a specific contract is to be performed outside the United States.

A number of commentators suggested various changes in the delegation procedures proposed by the Board. Since the Board is withdrawing the delegation, there is no need to consider these suggestions.

One commentator suggested that the reference in § 331.30(c) to the Assistant Secretary of Defense (Installations and Logistics) be changed to reflect organizational changes in the Department of Defense. This revision has been made.

PREAMBLE M

Preamble to Revision, 9-18-80

The material set forth below is the preamble to the revision and republication of Part 331, September 18, 1980, at 45 FR 62011. This preamble to the publication of September 18, 1980, is included as part of the administrative history of Part 331.

SUMMARY

On June 1, 1979, the Board published in the FEDERAL REGISTER proposed revisions to Parts 331, 332 and 351 of its regulations dealing with contract coverage and the filing of Disclosure Statements. Based on comments to its June 1 proposal, the Board made substantial modifications in the proposed revisions and republished the revised Parts again for comment on February 8, 1980. After considering the comments to the second publication and reviewing all suggestions from interested parties, the Board has determined that the revised regulations are ready for promulgation. It believes that the revised regulations will result in improved administration and will be more readily understood by parties subject to the regulations.

EFFECTIVE DATE

April 1, 1981.

SUPPLEMENTARY INFORMATION

In the FEDERAL REGISTER of June 1, 1979, (44 FR 31655) the CASB published for comment proposed revisions to Parts 331, 332 and 351 of its regulations. The revisions were made for the purpose of simplifying these parts of the regulations and to modify them where experience indicated that changes would be desirable. Thirty-six responses were received by the Board to its request for comments.

The Board after consideration of the comments modified its proposed revisions and again published the revised parts for comment in the FEDERAL REGISTER of February 8, 1980 (45 FR 8677). Twenty comments were received to the February publication. The Board wishes to thank all of the respondents for their constructive suggestions which were of substantial assistance to the Board in its review and revision of these parts.

In the February 8 proposal two areas of the regulations drew a substantial number of comments from the respondents, the exemption of firm fixed price contracts (FFPs) awarded without submission of cost data and the definition of "increased costs paid by the Government" as such may occur under FFPs after award. The Board's views on these two areas and on other comments received are as follows:

1. *Exemption.* Commentators generally endorsed the Board's proposal to exempt FFPs awarded without submission of any cost data. However, most commentators urged the exemption be expanded to require that cost data be certified or that the data have been relied on as the basis of price.

The Board is not persuaded that the suggested modifications should be made in describing those contracts which would be subject to this exemption. Situations occur in which cost data are submitted in support of a price but are not certified because the award is designated as adequate price competition. Whether the data are used in a particular case can be difficult to establish. The Board however is satisfied that such data would not be submitted unless they were to be used. Because of this and because of the administrative simplicity of the test, the Board believes that the circumstances which would support an exemption of certain FFPs being adopted today is appropriate.

One commentator opposed the establishment of this exemption on the grounds it provided a positive incentive for a potential contractor to seek to avoid submission of cost data. Controlling law and regulations establish the circumstances under which a potential contractor may be required to submit cost data to support a price proposal in a national defense procurement. In addition Government representatives have authority to act to assure that the Government's interests are properly protected. Consequently, whether a potential contractor may or may not have an incentive to avoid submitting cost data is not determinative as to whether such data are submitted. The Board believes that Government representatives, in cases where they deem it appropriate, will obtain whatever data they are entitled to. Nonetheless, the Board acknowledges that linking application of Cost Accounting Standards to submission of cost data could result in requests for waivers from the cost data submission requirements that would not be made if cost data alone were involved. In order to preclude this result the Board has revised the exemption so that contracts on which submission of cost data was avoided by obtaining a waiver of cost or pricing data requirements nonetheless remain subject to the Cost Accounting Standards requirements.

2. *"Increased costs paid" under FFPs after contract award.* In its February 8 proposal the Board deleted certain proposed revisions contained in its June 1, 1979 proposal concerning the adjustment of FFP contracts in view of the objections of most commentators to the proposed changes. The Board in its February proposal limited changes in the regulations affecting FFPs to a clarification in § 331.70(b) concerning the measurement of increased costs paid by the United States under those contracts. The modified § 331.70(b) paragraph was the subject of adverse comment by a majority of industry commentators who maintain that under FFP contracts once price is agreed to, there can be no increased cost paid by the U.S. attributed to any subsequent changes the contractor may make in its cost accounting practices.

The question of adjustment of FFPs has been the subject of extensive discussions since 1972. In its original promulgations the Board recognized that there was increased cost paid by the U.S. under a FFP contract if during the accumulating and reporting process the contractor adopted practices that reduced his cost allocations below the allocation determined during the estimating process. It is noted that in the proposed contract regulations published for comment on December 30, 1971, a provision the same in all essential aspects to the present § 331.70(b) was included. At that time no commentator questioned the applicability of CAS to FFPs.

The second sentence of Section (h)(1) of Pub. L. 91-379 is as follows:

> Such regulations shall require * * * a contract price adjustment, with interest, for any increased cost paid because of the defense contractor's failure to comply with * * * standards or to follow consistently his disclosed cost accounting practices * * * in pricing contract proposals and in accumulating and reporting contract performance cost data.

This provision prescribes price adjustments for all contracts where there is a failure to comply in pricing proposals and in accumulating and reporting costs. Since the Congress did not exclude FFP contracts when it provided for recovery of increased cost paid to the contractor because of a failure to comply or failure to follow, it was and still is incumbent on the Board to insure that, in the absence of an exemption, such recovery is accomplished. Pub. L. 87-653, Truth in Negotiations, provides that the price of a contract shall be adjusted to exclude any significant sum by which a firm fixed price was increased because the cost data furnished by the contractor, in essence, was insufficient to enable the Government to judge accurately the contractor's cost estimates used in negotiating. The Board's requirements for adjustments to firm fixed price contracts when there is a failure to follow the cost accounting practices on which price was based embody essentially the same measurement principle. The Board's requirements concerning fixed price contracts constitute a recognition of the fact that the price agreed to at the outset is higher than the price that would have been agreed to if the Government had known about the accounting change. This constitutes a constructive increase in the costs paid by the United States. In view of the foregoing, the Board's regulations will continue to require recovery of increased costs paid by the United States on FFPs. However, to emphasize that the contracting parties are the ones to determine what the contract price would have been and that there are no precise rules to be used in such determinations, further provision has been added to § 331.70(b).

(3) *Modification of § 331.70(f).* One commentator suggested that § 331.70(f) be modified to delete reference to "all affected contracting officers" and place the authority to effect agreement in the hands of one contracting officer delegated by affected agencies to handle CAS matters. In § 331.70(e) the Board urged that the contracting agencies designate such an individual and generally agencies have done so. However, this is a voluntary action of the agencies and the Board is not in a position to make it mandatory.

Two commentators urged § 331.70(f) be modified to refer to aggregate cost increases and offsets rather than deal with adjustments to individual contracts. In § 331.70 (e) and (f) the CASB has suggested techniques which it considers will permit substantially easier administration in situations in which a number of covered contracts may be involved. However, basic procurement statutes and Pub. L. 91-379 all deal with individual contracts and in the end adjustments must be made on an individual contract basis. Consequently, it is considered that reference to adjustments on an individual contract basis and allowance for offset among contracts where appropriate is the more precise way of discussing contract price adjustments.

(4) *Statement on Fairness.* One commentator requested the Board issue a statement on fairness in the application of its contract clause and related interpretations. The essence of the statement recommended would be that the results in any particular case arising from application of the Board's Standards, rules and regulations must be deemed "fair" in some general undefined sense by the negotiating parties or the Board's issuance may be disregarded. The Board's Restatement of Objectives, Policies and Concepts contains a statement that a Standard is fair when, in the Board's best judgment, it shows neither bias nor prejudice to either party. The Board views its rules and regulations on contracts and price adjustments in the same light. In any given case, the results of contract pricing may ultimately be regarded as fair or unfair by either or both parties to the contract because, on a case-by-case basis, fairness is viewed from the personal vantage point of the particular party. It is impossible to adopt such a subjective criteria and have meaningful Standards. Consequently any attempt to define "fairness" in the context of individual contract negotiations is inappropriate.

(5) *Miscellaneous.* There were various miscellaneous comments and suggestions on the Board's proposal to which the following comments are addressed:

(a) *Application of revised regulations.* Two commentators requested that the regulations, as revised by this promulgation, be applied to existing contracts. To the extent the Board has restated its interpretations to its regulations, such restatement would apply to existing contracts. However, other modifications will become effective only on the date specified in the revised regulations. This date is established so that sufficient lead time is available to procurement agencies to develop and publish any implementing regulations or instructions. The revised regulations other than restated interpretations will only apply to contracts and events which occur after the effective date of the regulation.

(b) *Section 351.120(a), Disclosure Statement revisions.* This paragraph was modified to provide that a Disclosure Statement must be revised when a change is made by the contractor whether or not the Government has agreed to the change. One commentator objected to this revision on the grounds it would increase the contractor's workload substantially. The change was made merely to clarify an existing requirement. It does not make a substantial change in the requirements set forth in the paragraph.

(c) *Increase the threshold for contract coverage and Disclosure Statement application.* Several contractors requested that the Board increase the threshold for contract coverage so as to make the application of CASB requirements effective only on contracts of $500,000 or more. Commentators also stated that the threshold for Disclosure Statement application should be increased. The Board has recently given consideration to both of these suggestions and is of the opinion that current thresholds are appropriate and no change in threshold application has been made in the regulations published today.

(d) *Deletion of post award disclosure under § 331.60.* One commentator objected to the deletion under § 331.60 of the provisions for post-award submission of Disclosure Statements. The Board considers the time currently provided under § 351.40 to be more than adequate for the preparation and submission of Disclosure Statements prior to award. Consequently, it considers that provisions for post-award submission is unnecessary.

(e) *"Cost to Complete" method of § 331.70(b).* One commentator urged that the Board provide under § 331.70(b) for the use of the "Cost of Complete" method of determining contract adjustments. It is considered that this paragraph, as revised, gives the contracting parties sufficient guidance with respect to the measurement of price impact. Consequently, the requested change has not been made.

(f) *Deletion of submission of disclosure statement of CASB.* Since the Board was receiving copies of disclosure statements to assist in its research in developing standards and since that development has been substantially completed, receipt by the Board of disclosure statements is unnecessary. Consequently, this requirement has been deleted.

Title 4 CFR Parts 331 and 332 are revised in their entirety and Part 351 is amended by revising §§ 351.30, 351.40, 351.60, 351.70, 351.80, and 351.120 and by deleting and reserving §§ 351.50 and 351.110 as follows:

PART 332—MODIFIED CONTRACT COVERAGE

Sec.
332.10 Purpose.
332.20 Definition.
332.30 Applicability.
332.40 [Reserved]
332.50 Contract clause.
332.51 Findings.
332.60 Disclosure requirements.
332.70 Interpretation.
332.80 Effective date.
PREAMBLES A—B

AUTHORITY: Sec. 103, 84 Stat. 796 (50 U.S.C. App. 2168).

SOURCE: 45 FR 62016, Sept. 18, 1980, unless otherwise noted.

NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles are intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (42 FR 45625, Sept. 12, 1977) is set forth in Preamble A of the supplement.

§ 332.10 Purpose.

The regulations contained in this part are promulgated to provide modified contract coverage for certain classes of business units.

§ 332.20 Definition.

The definitions set forth in § 331.20 of this chapter shall apply to this part.

§ 332.30 Applicability.

(a) Except for the award of a single covered contract of $10 million or more the provisions of this part may be applied in lieu of Part 331 of this chapter to any covered contract received by a business unit which in its immediately preceding cost accounting period received less than $10 million in awards of covered contracts: *Providing,* That the sum of such awards equals less than 10 percent of the business unit's total sales during that period.

(b) If in any cost accounting period the provisions of this part are applied to any one award to a business unit, they must be applied to all covered contracts awarded to that unit during that period, except under the following conditions. If the business unit receives a single contract award of $10 million or more, that contract must contain the clause set forth in § 331.50 of this chapter. Thereafter any covered contract awarded in the same cost accounting period must also contain that clause.

(c) Any covered contract awarded subject to this part shall remain subject thereto even if a portion of the contract is performed in a subsequent cost accounting period in which the business unit is exempt from the requirements of the Cost Accounting Standards Board or ineligible to use this part.

§ 332.40 [Reserved]

§ 332.50 Contract clause.

(a) Upon appropriate certification by the offeror that he is eligible and elects to use this part, the following clause shall be inserted in any resulting contract in lieu of the clause prescribed in § 331.50 of this chapter.

Disclosure and Consistency of Cost Accounting Practices

(a) The contractor, in connection with this contract shall: (1) Comply with the requirements of 4 CFR Parts 401, Consistency in Estimating, Accumulating and Reporting Costs, and 402, Consistency in Allocating Costs Incurred for the Same Purpose, in effect on the date of award of this contract.

(2) If it is a business unit of a company required to submit a Disclosure Statement, disclose in writing its cost accounting practices as required by regulations of the Cost Accounting Standards Board. If the contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets and commercial or financial information which is privileged and confidential, the Disclosure Statement will be protected and will not be released outside of the Government.

(3) Follow consistently, his cost accounting practices. A change to such practices may be proposed, however, by either the Government or the contractor, and the contractor agrees to negotiate with the Contracting Officer the terms and conditions under which a change may be made. After the terms and conditions under which the change is to be made have been agreed to, the change must be applied prospectively to this contract, and the Disclosure Statement if affected must be amended accordingly.

The contractor shall, when the parties agree to a change to a cost accounting practice and the contracting officer has made the finding required in § 332.51 of the Cost Accounting Standards Board's regulations, negotiate an equitable adjustment as provided in the changes clause of this contract. In the absence of the required finding no agreement may be made under this contract clause that will increase costs paid by the United States.

(4) Agree to an adjustment of the contract price or cost allowance, as appropriate, if he or a subcontractor fails to comply with the applicable Cost Accounting Standards or to follow any cost accounting practice and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States together with interest thereon computed at the rate determined by the Secretary of the Treasury pursuant to Pub. L. 92-41, 85 Stat. 97, or 7 percent per annum, whichever is less, from the time the payment by the United States was made to the time the adjustment is effected.

(b) If the parties fail to agree whether the contractor has complied with an applicable Cost Accounting Standard, rule or regulation or the Cost Accounting Standards Board and as to any cost adjustment demanded by the United States, such failure to agree shall be a dispute concerning a question of fact within the meaning of the disputes clause of this contract.

(c) The contractor shall permit any authorized representatives of the head of the agency, of the Cost Accounting Standards Board, or of the Comptroller General of the United States to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The contractor shall include in all negotiated subcontracts which he enters into the substance of this clause except paragraph (b) and shall require such inclusion in all other subcontracts of any tier, except that:

(1) If the subcontract is awarded to a business unit which pursuant to Part 331 is required to follow all Cost Accounting Standards, the clause entitled "Cost Accounting Standards" set forth in § 331.50 of the Board's regulations shall be inserted in lieu of this clause, or

(2) This requirement shall apply only to negotiated subcontracts in excess of $100,000 where the price negotiated is not based on

(i) Established catalog or market prices of commercial items sold in substantial quantities to the general public or

(ii) Price set by law or regulation, or

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a Cost Ac-

counting Standards clause by reason of § 331.30(b) of the Board's regulation.

§ 332.51 Findings.

Prior to making any equitable adjustment under subparagraph (3) of the contract clause set out in § 332.50 the contracting officer shall make a finding that the change is desirable and is not detrimental to the interests of the Government.

§ 332.60 Disclosure requirements.

General provisions concerning filing of a Disclosure Statement and the time at which such Disclosure Statement must be filed are set forth in Part 351 of this chapter.

§ 332.70 Interpretation.

(a) For the purpose of determining under § 332.30(a) whether the sum of covered contract awards equals less than 10 percent of the business unit's total sales, an order received by the one segment from another segment shall be treated in the same way that a subcontract award to the receiving segment would be treated. In measuring sales for a year, a transfer by one segment to another shall be deemed to be a sale by the transferor.

(b) Contracts subject to this Part 332 may be performed during a cost accounting period in which a subsequently awarded contract subject to Part 331 is also being performed. Compliance with the requirements established by Part 331 may compel the use of cost accounting practices for the subsequently awarded contract that are not required under this Part 332. Under these circumstances, the cost accounting practices applicable to contracts subject to this Part 332 need not be changed. Any resulting differences in practices between the contracts subject to this part and those subject to Part 331 of this chapter shall not constitute violations of Standard 401 or 402.

(c) In applying § 332.30(a), business units using Federal Management Circular 73-8 (Cost Principles for Educational Institutions) shall use the amount of current funds expenditures in lieu of total sales.

(d) The interpretation set forth in § 331.70 shall also apply to this part.

§ 332.80 Effective date.

Part 332, as amended, must be applied to contracts whose date of award is April 1, 1981 or if the contractor has submitted cost or pricing data, whose date of final agreement on price is after that date.

PREAMBLE A

Preamble to Original Publication 9-12-77

The material set forth below is the preamble to the original publication of Part 332, 42 FR 45625, Sept. 12, 1977.

CONTRACT COVERAGE, MODIFIED CONTRACT COVERAGE, BASIC REQUIREMENTS AND COST ACCOUNTING STANDARDS

This publication adds a new Part 332 and amends Parts 331, 351 and 403 of the Cost Accounting Standards Board's rules, regulations and Standards. The proposal to add Part 332 and to amend Parts 331 and 351 were published for comment in the February 16, 1977 FEDERAL REGISTER (42 FR 9389). The proposal to amend Part 403 was published for comment in the November 30, 1976 FEDERAL REGISTER (41 FR 52473). Appropriate periods for comment on the proposals were provided. Numerous and extensive comments were received concerning both proposals. The Board appreciates the interest expressed by the commentators and thanks them for their participation.

COMMENTS OF PARTS 332, 331 AND 351

GENERAL

Many commentators expressed general approval of the proposal to exempt certain businesses and provide modified coverage for others. Information available to the Board does not demonstrate that the benefits to be derived from applying all requirements to all contracts clearly outweigh the cost of requiring such application. Moreover the Board does not believe that many small companies with less sophisticated accounting systems and small accounting staffs can comply with the Board's requirements without experiencing inordinate difficulty and some cost. Under these circumstances, the Board has concluded that it is appropriate to remove completely the obligation of small businesses to comply with Standards, rules, and regulations of the Board. In reaching this conclusion the Board has also given some weight to the belief expressed by a few commentators that the prospect of having to comply with Board requirements has caused some companies to avoid Government contracts.

As noted by some commentators who opposed the Board's proposal, the granting of exemptions tends to reduce rather than increase uniformity of cost accounting practices because of the exemptions. In that sense the action may be viewed as not being in furtherance of that statutory goal which is set forth in Pub. L. 91-379. It has long been recognized that uniformity is an extremely important objective of the Board's actions. It is not, however, the only consideration. If there were any doubt on this point, the fact that the Law authorizes the Board to prescribe rules and regulations exempting contractors from its requirements should dispel that doubt. The Board believes that the action being taken is consistent with its statutory duties viewed as a whole even though uniformity among some business units will be reduced.

THRESHOLD DETERMINATIONS

Several commentators noted that the $10 million threshold provided in Part 332 would be based on all contracts subject to Cost Accounting Standards rather than being limited to national defense contracts and subcontracts. They noted that Pub. L. 91-379 does not apply to nondefense contracts and that such contracts are subject to Board Standards rules and regulations only to the extent that the Administrator of General Services has extended coverage to it. Because of this they urged that the calculation be made only on the basis of national defense contracts and subcontracts. This recommendation has been adopted by the Board.

The proposal to exempt all contracts under $500,000 was viewed as generally desirable by many commentators. Some recommended that $1 million or more be established as the minimum coverage level. However, some commentators opposed exempting small contracts of a contractor required to follow Standards on large contracts. They contended that once the contractor has to establish practices in compliance with Standards, there is no additonal burden involved in applying those practices to its small contracts. In any case it is unlikely that application of those practices could result in burdens that would be equal to those that would result from applying one set of cost accounting practices to large contracts and another set to small contracts. For this reason the Board has not adopted the proposal to exempt all contracts under $500,000. Instead the existing provisions providing for coverage of smaller contracts awarded to a business unit which has received an award of $500,000 or more are being retained.

One commentator noted that some contractors receive contract awards of $10 million or more every other year and few, if any, covered awards in the intervening years. The large contracts would not be subject to disclosure requirements or Standards under the February 16 proposal. The Board has remedied this problem by providing that any single contract award of $10 million or more is subject to all Standards and must be covered by a Disclosure Statement.

SMALL BUSINESS

Several commentators urged that all businesses which qualify as small business concerns under the rules and regulations of the Small Business Administration be exempted. The February 16, 1977 proposal would have provided such an exemption only for a small business which received less than $10 million in awards during its preceding fiscal year. Modified coverage would have been provided for other small businesses. Research indicates that there are very few companies which would fall into the category of small businesses receiving awards of $10 million or more. In the interest of using a single test, i.e., whether the contractor qualifies as a small business concern, rather than a dual test which would result only in a few small businesses being subject to modified coverage, the Board has adopted the recommendation to exempt all small business concerns. Research indicates that if this action had been applied to Federal Fiscal Year 1976 it would have resulted in exemption of 196 small business concerns which were doing business with the Department of Defense and which had $460 million of contracts of the type subject to Cost Accounting Standards. Consequently, on average, each small business concern would have a relatively small amount of covered contracts.

OTHER CATEGORIES

Various commentators renewed previous recommendations that the Board exempt other categories of contracts and contractors. The categories included colleges, universities, nonprofit organizations, hospitals, and Government-owned contractor-operated facilities. The Board has considered these recommendations and concluded that none of these categories should be exempted.

PART 332 ELIGIBILITY

The February 16 publication would require that a contractor have less than $10 million in covered contracts and that the covered contracts be less than 10% of total sales to be eligible for Part 332. In discussing this provision some commentators proposed a wide variety of tests in lieu of the tests proposed in that publication. Some suggested using only a dollar test or only a percentage test rather than both. The amounts recommended ranged up to $100 million and 50 percent of total sales. Some suggested using sliding scales to determine eligibility. None of the suggested tests appear more likely to achieve the purposes of the Board than the test originally proposed. The Board has therefore retained its initial proposal.

SCOPE OF PART 332

A number of commentators recommended that eligibility for Part 332 should result in complete exemption. Others recommended that requirement for compliance with Parts 401 and 402 be the only requirement and that the disclosure obligation be eliminated. The Board believes that substantical benefits may be derived by continuing to require compliance with Parts 401 and 402. There is nothing which suggests that compliance with the two Standards entails any significant cost. Consequently this requirement is being retained. According to information reported to the Board, adoption of Part 332 will relieve 264 segments of 131 contractors of the requirements to comply with all Standards but will remove only $405 million of contracts from full coverage.

DISCLOSURE STATEMENT REQUIREMENTS

Many commentators suggested that preparation of a Disclosure Statement was burdensome. They also contended that in the situation where a large commercial contractor receives only a few small contracts containing a Cost Accounting Standards clause the need for a Disclosure Statement appears to be minimal. Some asserted that adoption of the proposal to require a Disclosure Statement for all covered contracts would reduce the number of companies that would accept contracts subject to the Board's Standards, rules and regulations. The Board is persuaded that for the time being Disclosure Statements should not be required for all covered contracts. Accordingly it is not adopting the February 16 proposal. The Board is retaining the existing Disclosure Statement requirement provided in Part 351 except that a business unit will be required to submit a Disclosure Statement if it is a company or a segment of a company which received awards of national defense contracts subject to Cost Accounting Standards in excess of $10 million during its preceding cost accounting period rather than the preceding Federal fiscal year.

REVISIONS TO PART 351

Part 332 and the amendments to Part 331 generally will result in annual determinations being made of a contractor's obligation to follow Standards and to submit Disclosure Statements. The determination will be made on the basis of sales and awards data from the immediately preceding cost accounting period. The requirement to continue to submit a Disclosure Statement so long as the contractor has a contract subject to Cost Accounting Standards will no longer apply. Disclosure Statements must be maintained for and applied to only those contracts which were awarded during a cost accounting period in which the contractor met the filing requirements of § 351.40. Sections 351.40 and 351.50 have been revised to reflect this change.

SEGMENTS OF LARGE COMPANIES

A number of commentators sought to have small segments of large companies treated in the same way that small businesses are treated. In their view, small segments are competing in the same environment as small business and are operating with essentially similar capacity and resources. Therefore, such segments, they concluded, should be subject to the same rules as small business. The Board does not accept this line of reasoning. Even in those cases where a segment may appear to operate as a small business its status as a segment precludes it from being regarded in the same way. It has available to its capacities and resources of the company of which it is a part. Also the policy considerations of the Small Business Act have no applicability to segments of a larger company. Further, as a practical matter, the rules already exist in the Small Business Administration for identifying small business concerns. There are no comparable rules for identifying small segments.

As indicated by the February 16 proposal the Board nonetheless recognizes that segments which are engaged in primarily noncovered work should be eligible for modified coverage. This coverage is provided by Part 332. It will apply to segments which according to information submitted to the Board have average covered sales of approximately $1.4 million per segment. The relatively small amount of covered contract sales by each of these segments, the limited Government interest in the total business activity of the unit and the fact that the implementation and administration involves some cost lead to the conclusion that modified coverage is appropriate and sufficient to protect the interests of the Government.

SUMMARY

The results of the Board's adoption of Part 332 and amendment of Parts 331 and 351 are:

1. None of the Board's requirements apply to a business unit unless it has received an award of at least one covered contract of more than $500,000. Thereafter covered contracts of more than $100,000 are subject to the Board's requirements.

2. A Disclosure Statement must be submitted by any business unit receiving a covered contract if it is either a company which received net awards of negotiated national defense prime contracts and subcontracts subject to Cost Accounting Standards totaling $10 million or more in its preceding cost accounting period or a segment of such a company.

3. Contracts awarded to any business unit which received less than $10 million in awards of covered contracts in its preceding cost accounting period are subject to:

(a) Standards 401 and 402, if the dollar amount of such awards is equal to less than 10 percent of the business unit's total sales during that period; or

(b) All Standards, if the dollar amount of such awards is equal to 10 percent or more of the business unit's total sales during that period.

4. Any single award of a covered contract of $10 million or more is subject to all Standards and requires submission of a Disclosure Statement.

5. Contracts awarded to any business unit which received $10 million or more in awards of covered contracts during the preceding cost accounting period are subject to all Standards.

6. Notwithstanding the foregoing, all businesses which qualify as small business concerns under the rules and regulations of the Small Business Administration are exempt from all Cost Accounting Standards Board requirements.

BEST CO

COMMENTS ON PART 403

With respect to the amendment of Part 403, the November 30, 1976 proposal was to revise that Standard to make it applicable to any contract which was subject to Cost Accounting Standards generally. The amendment being promulgated today retains this concept. However, as recommended by a number of commentators, the Board deferred the promulgation of this amendment pending the amendments to Parts 331 and 351 and the addition of Part 332 discussed above.

The decision to extend the application of Part 403 to additional contractors was made on the basis of extensive research. This research included both those contractors who were already required to use Part 403 and those who were expected to use it as a result of this amendment. With respect to the current users, the Board is satisfied that this Standard has resulted in more equitable allocations, with little administrative effort in most cases. With respect to potential additional users, the research indicated that many of these would have to make few, if any, changes to comply with Part 403 and that the remainder could comply with little difficulty. The Board notes in addition, an independent study by the Conference Board which found that defense contractors who are using Part 403 for contract costing purposes are using the same allocation procedures for internal reporting purposes. According to the Conference Board, it was typical of these companies to allocate home office expenses on a blanket basis prior to the promulgation of Part 403. (Information Bulletin No. 17, February 1977.)

A number of commentators suggested various limitations for the application of Part 403. Some of these suggestions were expressed in general terms. Some of the commentators recommended, for example, that the requirement to use Part 403 should not be extended to "small contractors." Alternatively or additionally it was recommended that Part 403 should not be required for a large contractor with little work subject to Cost Accounting Standards. More specifically, recommendations were received to exempt those contractors with less than 10 percent of their revenue from Government work. Others recommended that contractors who have less than $10 million in contracts subject to Cost Accounting Standards should be exempt. The Board believes that the recommendations of this nature have been accommodated to the extent desirable and practical by the amendments to Parts 331 and 351 and the addition of Part 332 being promulgated today. Accordingly, any further exemption from Part 403, specifically, is considered to be unnecessary.

In publishing the proposed amendment to Part 403 in the FEDERAL REGISTER of November 30, 1976, the Board stated that there is evidence that almost all contractors who were required to make significant changes in their allocation practices as a result of Part 403 did so without undue trouble or expense. Several commentators questioned the Board's conclusion in this regard. The Board's conclusion was based in part on Staff research involving 147 home offices who now use Part 403 to allocate home office expenses. This research sought to determine, among other things, the administrative problems and expense involved in making allocations pursuant to Part 403. Government auditors reported that of the 147 home offices, only 4 had problems in developing the necessary data and that there was evidence of significant adminstrative costs at one of these four offices. In addition, evidence of significant administrative costs in making the allocations was found by the Government auditors at four other of the 147 home offices.

Some of the respondents who questioned the Board's conclusions regarding administrative problems and expense referred to an industry report on the economic impact of Cost Accounting Standards as support for this position. These respondents variously referred the Board to those sections of the report which summarized (i) contractor's appraisal of benefits from Part 403; (ii) the number of contractors who were required to make changes as a result of Part 403; (iii) the number of noncompliance notices issued in connection with Part 403;

and (iv) the increase and decrease in costs allocated to Government work as a result of CAS 403. Nothing in these sections, however, specifically addresses the question of administrative problems or expense involved in complying with Part 403.

Two associations reported that, contrary to the Board's findings, their member companies had experienced trouble and expense in complying with Part 403. These associations declined to identify the companies involved, the nature of the problems, or the amount of the expenses. Under these circumstances, there is no basis to alter the conclusion that contractors have been able to make changes required as a result of Part 403 without undue trouble or expense.

One commentator stated that it would not be desirable to make more contractors subject to Part 403 because he believes it to be defective, particularly with respect to its application to the allocation of state and local taxes. With respect to the application of the Standard to the allocation of state and local taxes specifically, the Board notes that it reached its conclusion on the basis of considerable research and extensive deliberation. Moreover, it has reexamined its conclusions, even after the promulgation of Part 403. Notwithstanding the views of the commentator, the Board continues of the view that the provision in question is proper. Accordingly, the Board does not agree that this Standard should not be extended to additional contractors because of the tax allocation provision.

EFFECTIVE DATE

The effective date of the regulations being published today is March 10, 1978. Pub. L. 91-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

PREAMBLE B

NOTE: For text of Preamble B to Part 332, see Preamble M to Part 331, published at 45 FR 62009, Sept. 18, 1980.

SUBCHAPTER D—[RESERVED]

SUBCHAPTER E—DISCLOSURE STATEMENT

PART 351—BASIC REQUIREMENTS

Sec.
351.20 Purpose.
351.30 Definitions.
351.40 Filing requirement.
351.60 Forms.
351.70 Submission.
351.80 Incorporation of disclosure statement.
351.90 Adequacy of Disclosure Statement.
351.100 Effect of filing Disclosure Statement.
351.120 Amendment of disclosure statement.
351.130 Instructions and information.
351.140 Disclosure Statement.
351.145 Disclosure statement—colleges and universities.

Appendix A—Principal Product or Service Code

Preambles A–G

Authority: Sec. 103, 84 Stat. 796 (50 U.S.C. App. 2168), unless otherwise noted.

Source: 38 FR 30728, Nov. 7, 1973, unless otherwise noted.

Editorial Notes 1: For a document affecting §§ 351.50, and 351.70, see 39 FR 44030, Dec. 20, 1974.

2. A supplement, consisting of the preambles to these regulations as they appeared in the Federal Register, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (37 FR 4139, February 29, 1972) is set forth in preamble A of the supplement. The preamble to an amendment affecting the original publication of this part is set forth in preamble B of the supplement.

Part 351 was revised at 38 FR 30725, November 7, 1973, with the exception of § 351.50(c) and the last sentence of § 351.70. The preambles to the revision of this part are set forth in preambles B and C.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 351.20 Purpose.

This regulation is promulgated pursuant to section 719 of the Defense Production Act of 1950, as amended by 84 Stat. 796 (Pub. L. 91-379), to provide the means by which affected persons can satisfy the requirements established by that law for disclosure of their cost accounting practices and to promulgate the Disclosure Statement form. The regulation also sets forth the administrative procedures to be followed by the Cost Accounting Standards Board and relevant Federal agencies in connection with such disclosures.

§ 351.30 Definitions.

The definitions set forth in § 331.20 of this chapter shall apply to this part.

(Sec. 719, Defense Production Act of 1950, as amended, Pub. L. 91-379 (50 U.S.C. App. 2168))

[45 FR 62017, Sept. 18, 1980]

Preamble: For preamble relating to § 351.30, see preamble M to Part 331.

§ 351.40 Filing requirement.

(a) *Who must file.* (1) Any defense contractor which, together with its segments, received net awards of negotiated national defense prime contracts and subcontracts subject to Cost Accounting Standards totaling more than $10 million in its most recent cost accounting period, must submit a completed Disclosure Statement as specified in paragraph (b)(1) of this section.

(2) Any business unit which receives a negotiated national defense contract or subcontract which is subject to Cost Accounting Standards and is for $10 million or more must submit a completed Disclosure Statement as specified in paragraph (b)(2) of this section.

(3) Except as provided in 4 CFR 331.30(b) or except where the price is based on (i) established catalog or market prices of commercial items sold in substantial quantities to the general public or (ii) prices set by regulation, a separate Disclosure Statement must be submitted covering the practices of each segment of a defense contractor whose costs included in the total price of any covered contract ex-

ceeds $100,000. If the cost accounting practices are identical for more than one segment of a contractor, only one statement need be submitted for those segments, but each such segment must be identified.

(4) Each corporate or other home office which allocates costs to one or more disclosing segments performing covered contracts shall file a Part VIII of the Disclosure Statement.

(b) *Time of Filing.* Any defense contractor required by paragraph (a)(1) of this section to file a Disclosure Statement must do so prior to award of the first covered contract received by the contractor or by a segment of such contractor in the cost accounting period immediately following the period in which the contractor receives awards totaling $10 million. If the first covered contract is received within 90 days of the start of the cost accounting period, the contractor is not required to file until the end of the 90 days.

(2) Any business unit required by paragraph (a)(2) of this section to submit a Disclosure Statement must do so as part of its proposal for such contract unless the business unit has already submitted a Disclosure Statement disclosing the practices used in the pricing of its proposal.

(3) A corporate or home office required by paragraph (a)(4) of this section to file a Disclosure Statement shall do so at the same time its disclosing segment files its Disclosure Statement.

(c) *Confidentiality of disclosure statement.* (1) If the business unit submitting a Disclosure Statement notifies the contracting agency and the CASB that the Disclosure Statement contains trade secrets and commercial or financial information which it regards as privileged and confidential, the Disclosure Statement will be protected and will not be released outside of the Government. (Persons submitting Disclosure Statements containing such information should place an appropriate legend on the face of the document at the time of submission.)

(2) If a subcontractor considers that the information in its Disclosure Statement is privileged and confidential and declines to provide it to the contractor or higher tier subcontractor, the contractor may authorize direct submission of that subcontractor's Disclosure Statement to the same Government offices to which the contractor was required to submit its Disclosure Statement.

(d) *Waiver.* In the event the agency head determines that it is impractical to secure a required Disclosure Statement, he may authorize award of a contract or subcontract without submission of a Disclosure Statement. He shall within 30 days thereafter submit a report to the Cost Accounting Standards Board setting forth all material facts.

(Sec. 719, Defense Production Act of 1950, as amended, Pub. L. 91-379 (50 U.S.C. App. 2168))

[45 FR 62017, Sept. 18, 1980]

PREAMBLE: For preamble relating to § 351.40, see preamble M to Part 331.

§ 351.60 Forms.

(a) For the convenience of persons required to submit Disclosure Statements, the Cost Accounting Standards Board has devised forms which should be used. Form No. CASB-DS-1 is for general use. Form No. CASB-DS-2 may be used by educational institutions operating FFRDCs. Copies of the form may be requested by relevant Federal agencies for distribution to affected contractors and subcontractors from the Administrative Officer of the Cost Accounting Standards Board, 441 G Street NW., Washington, DC 20548. If for any reason, copies of the form cannot be obtained, the required information shall be supplied in a form substantially in accord with the arrangement set forth in § 351.130.

(b) Foreign contractors and subcontractors who are required to submit a Disclosure Statement may, in lieu of filing a Form No. CASB-DS-1, make disclosure by use of a disclosure form prescribed by an agency of its Government, provided that the Cost Accounting Standards Board determines that the information disclosed by that means will satisfy the objectives of Pub. L. 91-379.

(Sec. 719, Defense Production Act of 1950, as amended, Pub. L. 91-379 (50 U.S.C. App. 2168))

[45 FR 62018, Sept. 18, 1980]

PREAMBLE: For preamble relating to § 351.60, see preamble M to Part 331.

§ 351.70 Submission.

Each national defense contractor shall submit a copy of each Disclosure Statement, and any amendments thereto in accordance with the method prescribed by each Federal agency for which the contractor is performing or proposes to perform contracts subject to the rules, regulations and standards of the Cost Accounting Standards Board.

(Sec. 719, Defense Production Act of 1950, as amended, Pub. L. 91-379 (50 U.S.C. App. 2168))

[45 FR 62018, Sept. 18, 1980]

PREAMBLE: For preamble relating to § 351.70, see preamble M to Part 331.

§ 351.80 Incorporation of disclosure statement.

Every solicitation for a contract which will be subject to the standards, rules, and regulations of the Cost Accounting Standards Board shall contain a provision allowing the contractor to identify and incorporate by reference, a Disclosure Statement already on file which will be applicable to that solicitation. Such identification and incorporation shall satisfy the requirement for disclosure as a condition of contracting. Agencies may, nonetheless, require submission of additional copies of such Disclosure Statement to the extent deemed necessary.

(Sec. 719, Defense Production Act of 1950, as amended, Pub. L. 91-379 (50 U.S.C. App. 2168))

[45 FR 62018, Sept. 18, 1980]

PREAMBLE: For preamble relating to § 351.80, see preamble M to Part 331.

§ 351.90 Adequacy of Disclosure Statement.

Federal agencies shall prescribe regulations by which each will determine that a Disclosure Statement has adequately disclosed the practices required to be disclosed by Cost Accounting Standards Board's standards, rules, and regulations. Agencies are urged to coordinate development of such regulations. The Disclosure Statement submitted to the Cost Accounting Standards Board in accordance with § 351.70, is for evaluation and development of Board programs only. Consequently, such submission to the Board does not satisfy the requirement for disclosure as a condition of contracting, nor does any action by the Board with respect to such statement constitute a finding of any kind regarding the adequacy of the statements as submitted.

§ 351.100 Effect of filing Disclosure Statement.

Unless the Federal agency involved provides otherwise either by regulation or by specific notice to the contractor involved, a Disclosure Statement submitted to the agency or incorporated by reference shall be presumed adequate to meet the requirement that disclosure be made as a condition of contracting. The fact that the condition of contracting has been met shall serve only to establish what the contractor's cost accounting practices are or are proposed to be. In the absence of specific regulation or agreement, a disclosed practice shall not, by virtue of such disclosure, be deemed to have been approved by the agency involved as a proper, approved or agreed practice for pricing proposals or accumulating and reporting contract performance cost data.

§ 351.120 Amendment of disclosure statement.

(a) Disclosure Statements must be amended when disclosed practices are changed to comply with new Cost Accounting Standards. The Statements must also be amended when practices are changed with or without agreement of the Government under the provisions of § 331.50(a)(4) (B) or (C) or § 332.50(a)(3).

(b) Amendments shall be submitted to the same offices, including the Cost Accounting Standards Board, to which submission would have to be made were an original Disclosure Statement being filed. Revised responses for Items 1.4.0 through 1.7.0, 8.1.0 or 8.2.0 must be submitted at the beginning of the contractor's fiscal year only if the response to an item in the Disclosure Statement on file requires a change. If the contractor's sales were such that it would check the same boxes in the Disclosure Statement, resubmission of responses concerning these particular items is not required.

(c) For each revision of the Disclosure Statement (addition, change or deletion), only the pages containing such revision shall be resubmitted. Each resubmission shall include a new cover sheet and a signed certification. In the first line of Item 0.4 of the cover sheet, companies shall enter the date of the revision. On the next line of Item 0.4 the date of the last cover sheet that was submitted shall be entered. The numbers of the pages being revised and submitted with the cover sheet shall be entered immediately above the certification. The upper right corner of each revised page being submitted shall be marked "Revised" and dated with the date shown in the first line of Item 0.4. Companies shall enter in the right margin of each page, an asterisk (*) alongside each line containing a revision. For continuation sheets, asterisks may be used in the right margin to identify revised material. Agencies may prescribe criteria under which submission of a complete, updated Disclosure Statement will be required.

(Sec. 719, Defense Production Act of 1950, as amended, Pub. L. 91-379 (50 U.S.C. App. 2168))

[45 FR 62018, Sept. 18, 1980]

PREAMBLE: For preamble relating to § 351.120, see preamble M to Part 331.

§ 351.130 Instructions and information.

The following instructions and information shall be used by persons completing Disclosure Statements.

INSTRUCTIONS AND INFORMATION

(a) This disclosure statement has been designed to meet the requirements of Pub. L. 91-379, and persons completing it are to describe their contract cost accounting practices. For timing of requirement to file a disclosure statement, see § 351.40. A statement must be submitted by all defense contractors who enter into negotiated national defense contracts with the United States in excess of $100,000 other than contracts where the price negotiated is based on (1) established catalog or market prices of commercial items sold in substantial quantities to the general public, or (2) prices set by law or regulation, or contracts exempt under the provisions of 4 CFR 331.30(b). A separate disclosure statement must be submitted covering the practices of each of the contractor's profit centers, divisions, or similar organizational units, whose costs included in the total price of any contract exceed $100,000, except where such costs are based on (i) established catalog or market prices of commercial items sold in substantial quantities to the general public, or (ii) prices set by law or regulation, or contracts exempt under the provisions of 4 CFR 331.30(b). If the cost accounting practices under contracts are identical for more than one organizational unit, then only one statement need be submitted for those units, but each such organizational unit must be identified. A disclosure statement will also be required for each corporate or group office when costs are allocated to one or more corporate segments performing contracts covered by Pub. L. 91-379, but only Part VIII of the statement need be completed.

(b) The statement must be signed by an authorized signatory of the reporting unit.

(c) The disclosure of a cost accounting practice by a contractor does not determine the allowability of particular items of cost. Irrespective of the practices disclosed by a contractor, the question of whether or not, or the extent to which, a specific element of cost is allowed under a contract remains for consideration in each specific instance. Contractors are cautioned that the determination of the allowability of cost items will remain a responsibility of the contracting officers pursuant to the provisions of the applicable procurement regulations.

(d) Unless the Federal agency involved provides otherwise, either by regulation or by specific notice to the contractor involved, a Disclosure Statement submitted to the agency or incorporated by reference should be presumed adequate to meet the requirement that disclosure be made as a condition of contracting. In the absence of specific regulations or agreement, a disclosure practice should not, by virtue of such disclosure, be deemed to have been approved by the agency involved as a proper, approved, or agreed practice for pricing proposals or accumulating and reporting contract performance cost data.

(e) The individual Disclosure Statement may be used in audits of contracts or in negotiation of prices leading to contracts. The authority of the audit agencies and the contracting officers is in no way abrogated by the material presented by the contractor in his Disclosure Statement. Contractors are cautioned that their disclosures in response to the items herein must be complete and accurate; the practices disclosed may have a significant impact on ways in which contractors will be required to comply with Cost Accounting Standards.

(f) This Disclosure Statement should be answered by checking the appropriate box or inserting the applicable Code letter which most nearly describes the reporting unit's cost accounting practices. Part I of the statement asks for general information concerning the reporting unit. Part VIII covers Corporate and Group (Intermediate) offices whose costs are allocated to one or more segments performing contracts covered by Pub. L 91-379. Part VIII should be completed by each such office, and care should be taken to insure proper identification of such offices on the cover of the Disclosure Statement. In short, while a Corporation or group office may have more than one reporting unit submitting Disclosure Statements, only one statement need be submitted to cover the Corporate or Group Office operations.

(g) A number of questions in this statement may need narrative answers requiring more space than is provided. In such instances, the reporting unit should use the continuation sheets provided or a facsimile thereof. The number of the question involved should be indicated and the same coding required to answer the questions in the statement should be used in presenting the answer in the continuation sheet. The reporting unit should indicate on the last continuation sheet used, the number of such sheets that were used.

(h) Contractors to whom Pub. L. 91-379 is applicable are required to follow consistently their disclosed practices in pricing contract proposals and in accumulating and reporting contract performance cost data. If deviation from disclosed practices results in increased costs being paid by the Government, contractors will be required to repay to the Government the amount of the increased costs together with interest charges.

(i) Pub. L. 91-379 contains an access to records clause, section 719(j) of the law states:

"For the purpose of determining whether a defense contractor or subcontractor has complied with duly promulgated cost accounting standards and has followed consistently his disclosed cost accounting practices, any authorized representative of the head of the agency concerned, of the Board, or of the Comptroller General of the United States shall have the right to examine and make copies of any documents, papers, or records of such contractor or subcontractor relating to compliance with such cost accounting standards and principles."

[38 FR 30725, Nov. 7, 1973, as amended at 39 FR 44391, Dec. 12, 1974]

PREAMBLES: For preambles relating to § 351.130, see preambles C and E of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 351.140 Disclosure Statement.

The data which are required to be disclosed are set forth in detail in the Disclosure Statement form CASB-DS-1 which will be devised by the Cost Accounting Standards Board and will be arranged substantially as set forth below. For the form to be used by colleges and universities, see § 351.145.

NOTE: Forms CASB-DS-1 and CASB-DS-2, referred to in §§ 351.140 and 351.145, respectively, when revised, will be modified in accordance with the modifications to 4 CFR 351.130.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	COVER SHEET AND CERTIFICATION

0.1 Company or Reporting Unit.

Name

Street Address

City, state, & zip code

Division or subsidiary of
(if applicable)

0.2 Reporting Unit is: (Check one.)

A. [ ] Corporate (Home) office B. [ ] Group office

C. [ ] Division or subsidiary D. [ ] Other

0.3 Official to Contact Concerning this Statement.

Name and title

Phone number (incl. area code and extension)

0.4 Date of:

This statement

Most recent prior statement

CERTIFICATION

I certify that to the best of my knowledge and belief this Statement is the complete and accurate disclosure as of the above date by the above-named organization of its cost accounting practices, as required by the Disclosure Regulation of the Cost Accounting Standards Board under 50 U.S.C. App. 2168, Public Law 91-379, (4 CFR 351).

(Name)

(Title)

- THE PENALTY FOR MAKING A FALSE STATEMENT IN THIS DISCLOSURE IS PRESCRIBED IN 18 U.S.C. 1001

FORM CASB-DS-1

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	INDEX

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Continuation Sheet

FORM CASB-DS-1

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART I - GENERAL INFORMATION

Item No.	ITEM DESCRIPTION

Instructions for Part I

Sales data for this part should cover the most recently completed fiscal year of the reporting unit. "Government Sales" includes sales under both prime contracts and subcontracts. "Annual Total Sales" includes intracorporate transactions. Educational institutions may skip Items 1.4.0 and 1.6.0, and consider sales as used in Items 1.5.0 and 1.7.0 to refer to research revenues.

Estimates are permitted for Items 1.4.0 through 1.7.0.

1.1.0 Type of Business Entity of Which the Reporting Unit is a Part. (Check one.)

A. ☐ Corporation B. ☐ Partnership
C. ☐ Proprietorship D. ☐ Not-for-profit organization
E. ☐ Joint venture F. ☐ Educational institution

1.2.0 Predominant Type of Government Sales. (Check one.)

A. ☐ Manufacturing B. ☐ Research and Development
C. ☐ Construction D. ☐ Services
Y. ☐ Other (specify) ______________________

1.3.0 Principal Product or Service Sold to the Government. (Specify name of product or service and enter code from Instructions.)

Name ______________________ Code ☐☐☐☐☐

1.4.0 Annual Total Sales (Government and Commercial). (Check one.)

A. ☐ Less than $1 million B. ☐ $1-$10 million C. ☐ $11-$25 million
D. ☐ $26-$50 million E. ☐ $51-$100 million F. ☐ $101-$200 million
G. ☐ $201-$500 million H. ☐ Over $500 million

BEST COPY

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART I - GENERAL INFORMATION
Item No.	**ITEM DESCRIPTION**
1.5.0	Annual Total Government Sales. (Check one.) A. ☐ Less than $1 million B. ☐ $1-$10 million C. ☐ $11-$25 million D. ☐ $26-$50 million E. ☐ $51-$100 million F. ☐ $101-$200 million G. ☐ $201-$500 million H. ☐ Over $500 million
1.6.0	Government Sales (Item 1.5.0) as Percentage of Total Sales (Item 1.4.0). (Check one.) A. ☐ Less than 10% B. ☐ 10%-50% C. ☐ 51%-80% D. ☐ 81%-95% E. ☐ Over 95%
1.7.0	Government Subcontract Sales as Percentage of Total Government Sales (Item 1.5.0). (Check one.) A. ☐ Less than 10% B. ☐ 10%-50% C. ☐ 51%-80% D. ☐ 81%-95% E. ☐ Over 95%
1.8.0	Description of Your Cost Accounting System for Government Contracts and Subcontracts. (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.) A. ☐ Standard costs - Job order B. ☐ Standard costs - Process C. ☐ Actual costs - Job order D. ☐ Actual costs - Process Y. ☐ Other(s) (Describe on a continuation sheet.)
1.9.0	Integration of Cost Accounting with Financial Accounting. The cost accounting system is: (Check one. If B or C is checked, describe on a continuation sheet the costs which are accumulated on memorandum records.) A. ☐ Integrated with financial accounting records (Subsidiary cost accounts are all reconcilable to general ledger control accounts.)

FORM CASB-DS-1 - 2 -

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART I - GENERAL INFORMATION

Item No.	ITEM DESCRIPTION

1.9.0 Continued

B. [ ] Not integrated with financial accounting (Cost data are accumulated on memorandum records.)

C. [ ] Combination of A and B above

1.10.0 Unit or Job Costs. Is your cost accounting system capable of producing unit or job lot costs during contract performance? (Check one.)

A. [ ] Yes (If Yes, describe on a continuation sheet the method used or which could be used to arrive at such costs.)

B. [ ] No (Interim repricing not involved.)

C. [ ] No (Interim repricing involved. Describe on a continuation sheet the manner in which interim repricing is developed.)

1.11.0 Year, Month, Day on Which Your Most Recent Fiscal Year Ended. (Enter in blocks below. Use numeric terms, e.g., 710630 for June 30, 1971; 711231 for December 31, 1971.)

☐☐☐☐☐☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION

Instructions for Part II

This part covers three major elements of direct costs, i.e., Direct Materials, Direct Labor, and Other Direct Costs. It is not the intent here to spell out or define the three elements of direct costs.

Rather, contractors should disclose practices based on their own definitions of what costs are, or will be, charged directly to Government contracts or similar cost objectives as Direct Materials, Direct Labor, or Other Direct Costs. For example, some contractors may charge or classify purchased labor of direct nature, as "Direct Materials" for purposes of pricing proposals, requests for progress payments, claims for cost reimbursement, etc.; some other contractors may classify the same cost as "Direct Labor," and still others as "Other Direct Costs." In these circumstances, it is expected that contractors will disclose practices consistent with their own classifications of Direct Materials, Direct Labor, and Other Direct Costs.

2.1.0 Description of Direct Materials.

Direct Materials as used here are not limited to those items of materials actually incorporated into the end product; they also include materials, consumable supplies, and other costs when charged to Government contracts or similar cost objectives as Direct Materials.

(Describe on a continuation sheet the principal classes of materials and service costs which are charged as direct materials; group the materials and service costs by those which are incorporated in an end product and those which are not.)

2.2.0 Method of Charging Direct Materials.

2.2.1 Direct Charge Not Through an Inventory Account at: (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.)

A. ☐ Standard costs (Describe the type of standards used, e.g., current standards, basic standards, etc., on a continuation sheet.)

B. ☐ Actual costs

Y. ☐ Other(s) (Describe on a continuation sheet.)

Z. ☐ Not applicable

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 91-379

PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION

2.2.2 Charged from Central or Common, Company-owned Inventory Account at: (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.)

A. [ ] Standard costs (Describe the type of standards used on a continuation sheet.)
B. [ ] Average costs
C. [ ] First in, first out
D. [ ] Last in, first out
Y. [ ] Other(s) (Describe on a continuation sheet.)
Z. [ ] Not applicable

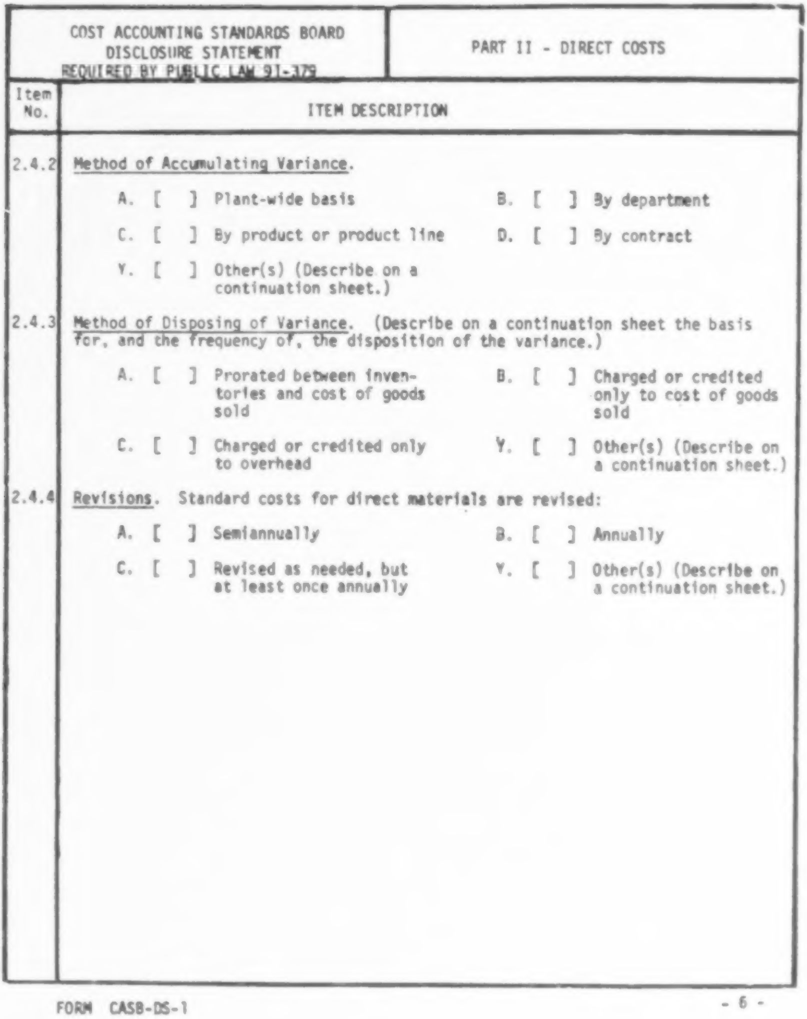
2.3.0 Timing of Charging Direct Materials Incorporated in End Product. (Check the appropriate block(s) to indicate the point in time at which materials incorporated in the end product are charged to Government contracts or similar cost objectives, and if more than one block is checked, explain on a continuation sheet.)

A. [ ] When orders are placed
B. [ ] When material is received, or when fabricated, if fabricated in-house
C. [ ] When material is issued or released to jobs
D. [ ] When consumed or incorporated in end product
E. [ ] When invoices are vouchered or paid
Y. [ ] Other(s) (Describe on a continuation sheet.)
Z. [ ] Not applicable

2.4.0 Variances from Standard Costs for Direct Materials. (Do not complete this item unless you use a standard cost method, i.e., you have checked Block A of Item 2.2.1 or 2.2.2. Check the appropriate block(s) in Items 2.4.1, 2.4.2, 2.4.3 and 2.4.4, and if more than one block is checked, explain on a continuation sheet.)

2.4.1 Type of Variance.

A. [ ] Price
B. [ ] Usage
C. [ ] Combined (A and B)
Y. [ ] Other(s) (Describe on a continuation sheet.)



COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION
2.4.2	Method of Accumulating Variance. A. [ ] Plant-wide basis — B. [ ] By department C. [ ] By product or product line — D. [ ] By contract Y. [ ] Other(s) (Describe on a continuation sheet.)
2.4.3	Method of Disposing of Variance. (Describe on a continuation sheet the basis for, and the frequency of, the disposition of the variance.) A. [ ] Prorated between inventories and cost of goods sold — B. [ ] Charged or credited only to cost of goods sold C. [ ] Charged or credited only to overhead — Y. [ ] Other(s) (Describe on a continuation sheet.)
2.4.4	Revisions. Standard costs for direct materials are revised: A. [ ] Semiannually — B. [ ] Annually C. [ ] Revised as needed, but at least once annually — Y. [ ] Other(s) (Describe on a continuation sheet.)

FORM CASB-DS-1 - 6 -

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 91-379

PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION

2.5.0 Method of Charging Direct Labor. (Check the appropriate block(s) for each Direct Labor Category to show how such labor is charged to Government contracts or similar cost objectives, and if more than one block is checked, explain on a continuation sheet. Also describe on a continuation sheet the principal classes of labor or costs that are, or will be, included in Manufacturing Labor, Engineering Labor, and Other Direct Labor, as applicable.)

		Direct Labor Category		
		Manufacturing (1)	Engineering (2)	Other Direct (3)
A.	Individual/actual rates	☐	☐	☐
B.	Average rates (Describe the type of average rates on a continuation sheet.)	☐	☐	☐
C.	Standard costs/rates (Describe the type of standards used on a continuation sheet.)	☐	☐	☐
Y.	Other(s) (Describe on a continuation sheet.)	☐	☐	☐
Z.	Labor category is not applicable	☐	☐	☐

2.6.0 Variances from Standard Costs for Direct Labor. (Do not complete this item unless you use a standard cost/rate method, i.e., you have checked Block C of Item 2.5.0 for any direct labor category. Check the appropriate block(s) in each column of Items 2.6.1, 2.6.2 and 2.6.3, and in Item 2.6.4. If more than one is checked, explain on a continuation sheet.)

2.6.1 Type of Variance.

		Direct Labor Category		
		Manufacturing (1)	Engineering (2)	Other Direct (3)
A.	Rate	☐	☐	☐
B.	Efficiency	☐	☐	☐
C.	Combined (A and B)	☐	☐	☐

FORM CASB-DS-1

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION			
2.6.1	Continued			
	Y. Other(s) (Describe on a continuation sheet.)	☐	☐	☐
	Z. Labor category is not applicable	☐	☐	☐
2.6.2	Method of Accumulating Variance.			
		Direct Labor Category		
		Manufacturing (1)	Engineering (2)	Other Direct (3)
	A. Plant-wide basis	☐	☐	☐
	B. By department	☐	☐	☐
	C. By product or product line	☐	☐	☐
	D. By contract	☐	☐	☐
	Y. Other(s) (Describe on a continuation sheet.)	☐	☐	☐
	Z. Labor category is not applicable	☐	☐	☐
2.6.3	Method of Disposing of Variance. (Describe on a continuation sheet the basis for, and the frequency of, the disposition of the variance.)			
		Direct Labor Category		
		Manufacturing (1)	Engineering (2)	Other Direct (3)
	A. Prorated between inventories and cost of goods sold	☐	☐	☐
	B. Charged or credited only to cost of goods sold	☐	☐	☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION

2.6.3 Continued

C. Charged or credited only to overhead	☐	☐	☐
Y. Other(s) (Describe on a continuation sheet.)	☐	☐	☐
Z. Labor category is not applicable	☐	☐	☐

2.6.4 Revisions. Standard costs for direct labor are revised:

A. ☐ Semiannually
B. ☐ Annually
C. ☐ Revised as needed, but at least once annually
Y. ☐ Other(s) (Describe on a continuation sheet.)

2.7.0 Credits to Contract Costs. When Government contracts or similar cost objectives are credited for the following circumstances, are the rates of direct labor, direct materials, other direct costs and applicable indirect costs always the same as those for the original charges? (Check one block for each circumstance, and for each "No" answer, explain on a continuation sheet how the credit differs from original charge.)

Circumstance	A. Yes	B. No	Z. Not Applicable
(a) Transfers to other jobs/contracts	☐	☐	☐
(b) Unused or excess materials remaining upon completion of contract	☐	☐	☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART II - DIRECT COSTS

Item No.	ITEM DESCRIPTION

2.8.0 Interorganizational Transfers.

This item is directed only to those materials, supplies, and services which are, or will be, transferred to you from divisions, subsidiaries, or affiliates under common control with you.

(Check the appropriate block(s) in each column to indicate the basis used by you as transferee to charge the cost or price of interorganizational transfers of materials, supplies, and services to Government contracts or similar cost objectives. If more than one block is checked, explain on a continuation sheet. Full cost means the cost incurred as set forth in ASPR 15-205.22(e) or other pertinent procurement regulations.)

Basis	Materials (1)	Supplies (2)	Services (3)
A. At full cost excluding transferor's general and administrative (G&A) expenses	☐	☐	☐
B. At full cost including transferor's G&A expenses	☐	☐	☐
C. At full cost (A or B above) plus a markup percentage	☐	☐	☐
D. At established catalog or market price or prices based on adequate competition	☐	☐	☐
Y. Other(s) (Describe on a continuation sheet.)	☐	☐	☐
Z. Interorganizational transfers are not applicable	☐	☐	☐

FORM CASB-DS-1 - 10 -

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART III - DIRECT VS. INDIRECT

Item No.	ITEM DESCRIPTION

3.1.0 Criteria for Determining How Costs are Charged to Government Contracts or Similar Cost Objectives. (Describe on a continuation sheet your criteria for determining whether costs are charged directly or indirectly.)

3.2.0 Treatment of Costs of Specified Functions, Elements of Cost, or Transactions. (For each of the functions, elements of cost or transactions listed in Items 3.2.1, 3.2.2, and 3.2.3, enter one of the Codes A through F, or Y, to indicate how the item is treated. Enter Code Z in those blocks that are not applicable to you. Also, specify the name(s) of the indirect pool(s) for each function, element of cost, or transaction Coded E or F. If Code E, Sometimes direct/Sometimes indirect, is used and if there is a deviation from the criteria described in response to Item 3.1.0, explain on a continuation sheet the circumstances involved which cause the deviation.)

Treatment Code

A. Direct material
B. Direct labor
C. Direct material and labor
D. Other direct costs
E. Sometimes direct/Sometimes indirect
F. Indirect only
Y. Other(s) (Describe on a continuation sheet.)
Z. Not applicable

3.2.1 Functions, Elements of Cost, or Transactions

Relative to Direct Materials

Functions, Elements of Cost, or Transactions	Treatment Code	Name of Pool(s)
(a) Cash discounts on purchases	[ ]	________________
(b) Freight in	[ ]	________________
(c) Income from sale of scrap	[ ]	________________
(d) Income from sale of salvage	[ ]	________________
(e) Incoming material inspection	[ ]	________________
(f) Inventory adjustments	[ ]	________________
(g) Purchasing	[ ]	________________
(h) Trade discounts, refunds, rebates, and allowances on purchases	[ ]	________________

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379		PART III - DIRECT VS. INDIRECT	
Item No.	ITEM DESCRIPTION		
3.2.2	Functions, Elements of Cost, or Transactions	Treatment Code	Name of Pool(s)
	Relative to Direct Labor		
	(a) Health insurance	[ ]	______
	(b) Holiday differential (premium pay)	[ ]	______
	(c) Overtime premium pay	[ ]	______
	(d) Pension costs	[ ]	______
	(e) Shift premium pay	[ ]	______
	(f) Training	[ ]	______
	(g) Travel and subsistence	[ ]	______
	(h) Vacation pay	[ ]	______
3.2.3	Functions, Elements of Cost, or Transactions		
	Miscellaneous		
	(a) Design engineering (in-house)	[ ]	______
	(b) Drafting (in-house)	[ ]	______
	(c) Computer operations (in-house)	[ ]	______
	(d) Contract administration	[ ]	______
	(e) Freight out (finished product)	[ ]	______
	(f) Line (or production) inspection	[ ]	______
	(g) Packaging and preservation	[ ]	______
	(h) Preproduction costs and start-up costs	[ ]	______
	(i). Production shop supervision	[ ]	______

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FORM CASB-DS-1

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 91-379

PART III - DIRECT VS. INDIRECT

Item No.	ITEM DESCRIPTION		Treatment Code	Name of Pool(s)
3.2.3	Continued			
	(j)	Professional services (consultant fees)	[ ]	____________
	(k)	Purchased labor of direct nature (on premises)	[ ]	____________
	(l)	Purchased labor of direct nature (off premises)	[ ]	____________
	(m)	Rearrangement costs	[ ]	____________
	(n)	Rework costs	[ ]	____________
	(o)	Royalties	[ ]	____________
	(p)	Scrap work	[ ]	____________
	(q)	Special test equipment (as defined in ASPR 15-205.40 or other pertinent procurement regulations)	[ ]	____________
	(r)	Special tooling (as defined in ASPR 15-205.40 or other pertinent procurement regulations)	[ ]	____________
	(s)	Subcontract costs	[ ]	____________
	(t)	Warranty costs	[ ]	____________

3.3.0 Other Costs Charged Direct to Contracts. (Describe on a continuation sheet all other significant functions, elements of cost, or transactions charged to Government contracts or similar cost objectives as direct material, direct labor or other direct costs. Do not include functions or costs covered in Items 2.1.0, 2.5.0, and 3.2.0 which are always charged direct. Describe also whether there are any deviations from the criteria set out in Item 3.1.0 with respect to any continuation sheet items.)

FORM CASB-DS-1 - 13-

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No.	ITEM DESCRIPTION

Instructions for Part IV

For the purpose of this part, indirect costs have been divided into three categories: (i) manufacturing, engineering, and comparable indirect costs, (ii) general and administrative (G&A) expenses, and (iii) service center costs, as defined in Item 4.3.0. The term "overhead," as used in this part, refers only to the first category of indirect costs.

The following Allocation Base Codes are provided for use in connection with Items 4.1.0, 4.2.0 and 4.3.0. Educational institutions, to which ASPR XV, Part 3 applies, may enter Code Y for Items 4.1.0(n), 4.2.0(n) and 4.3.0(1), and describe on a continuation sheet the indirect cost pools and the bases for allocating such pools of expenses to Government contracts or similar cost objectives.

A. Sales
B. Cost of sales
C. Cost input (direct material, direct labor, other direct costs and applicable overhead)
D. Total cost incurred (cost input plus G&A expenses)
E. Prime cost (direct material, direct labor and other direct cost)
F. Processing or conversion cost (direct labor and applicable overhead)
G. Direct labor dollars
H. Direct labor hours
I. Machine hours
J. Usage
K. Unit of product
L. Direct material cost
M. Total payroll dollars (direct and indirect employees)
N. Headcount or number of employees (direct and indirect employees)
O. Square feet
Y. Other(s) or more than one basis (Describe on a continuation sheet.)
Z. Pool not applicable

4.1.0 Overhead Pools and Allocation Bases. (Enter for each type of overhead pool one of the Allocation Base Codes A through O or Y, to indicate the basis for allocating such pool of expenses to Government contracts or similar cost objectives, i.e., allocation to these final cost objectives without any intermediate allocations. Enter Code Z in those blocks for types of pools that are not applicable to the reporting unit; however, if you use a single plant-wide pool, Lines (b) through (n) may be left blank.)

Type of Pool	Allocation Base Code
(a) Single, plant-wide pool (If an entry other than "Z" is made here, skip to Item 4.2.0)	[ ]

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No.	ITEM DESCRIPTION
4.1.0	Continued

	Type of Pool	Allocation Base Code
(b)	Manufacturing	[ ]
(c)	Engineering	[ ]
(d)	Manufacturing and Engineering	[ ]
(e)	Tooling	[ ]
(f)	Off-site or out-plant (geographical pool)	[ ]
(g)	Field service	[ ]
(h)	Material handling	[ ]
(i)	Departmental/shop	[ ]
(j)	Subcontract administration	[ ]
(k)	Use and occupancy	[ ]
(l)	Quality control	[ ]
(m)	Fringe benefits	[ ]
(n)	Other pools (Enter Code Y on this line if other pools are used and identify on a continuation sheet each such pool and its Allocation Base Code. If no other pools are used, enter Code Z.)	[ ]

4.2.0 Reporting Unit's G&A Pools and Allocation Bases. (Enter for each type of G&A pool one of the Allocation Base Codes A through O, or Y, listed on Page 14 to indicate the basis for allocating G&A to Government contracts or similar cost objectives, i.e., allocation to these final cost objectives without any intermediate allocations. Enter Code Z in those blocks for types of pools that are not applicable to the reporting unit; however, if an entry other than "Z" is made on Line (a), (b), (c) or (d), Lines (e) through (n) may be left blank.)

	Type of Pool	Allocation Base Code
(a)	Single G&A pool only	[ ]

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No.	ITEM DESCRIPTION
4.2.0	Continued

No Separate G&A Pool	Allocation Base Code
(b) Combined with single, plant-wide overhead pool	[ ]
(c) Combined with manufacturing overhead	[ ]
(d) Combined with engineering overhead	[ ]
More Than One Pool	
(e) General and administrative	[ ]
(f) Commercial - General and administrative	[ ]
(g) Government - General and administrative	[ ]
(h) Selling or marketing expense	[ ]
(i) Independent research and development (IR&D) costs	[ ]
(j) Bidding and proposal (B&P) costs	[ ]
(k) IR&D and B&P costs	[ ]
(l) Spares administration	[ ]
(m) Corporate or home office expense	[ ]
(n) Other pools (Enter Code Y on this line if other pools are used and identify on a continuation sheet each such pool and its Allocation Base Code. If no other pools are used, enter Base Code Z.)	[ ]

4.3.0 Service Centers and Allocation Bases.

Service centers are departments or other functional units which perform specific technical and/or administrative services for the benefit of other units within a reporting unit.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No.	ITEM DESCRIPTION

4.3.0 Continued

Category Code

Generally, costs incurred by such centers are, or can be, charged or allocated (i) partially to specific final cost objectives as direct costs and partially to other indirect cost pools (such as a manufacturing overhead pool) for subsequent reallocation to several final cost objectives, referred to herein as Category "A", and (ii) only to several other indirect cost pools (such as manufacturing overhead pool, engineering overhead pool and G&A expense pool) for subsequent reallocation to several final cost objectives, referred to herein as Category "B".

Rate Code

Some service centers may use predetermined billing or costing rates to charge or allocate the costs (Rate Code A) while others may charge or allocate on an actual basis (Rate Code B).

(Enter in Column (1) for each service center, Code A or B to indicate the category of pool. Enter in Column (2) one of the Allocation Base Codes A through O, or Y, listed on Page 14, to indicate the basis of charging or allocating service center costs. Enter in Column (3) Rate Code A or B to describe the costing method used. Enter Code Z in Column (1) only, if any service center is not applicable to the reporting unit.)

	Service Center	Category Code (1)	Allocation Base Code (2)	Rate Code (3)
(a)	Scientific computer operations	[ ]	[ ]	[ ]
(b)	Business data processing	[ ]	[ ]	[ ]
(c)	Photography services	[ ]	[ ]	[ ]
(d)	Reproduction services	[ ]	[ ]	[ ]
(e)	Art services	[ ]	[ ]	[ ]
(f)	Technical typing services	[ ]	[ ]	[ ]
(g)	Communication services	[ ]	[ ]	[ ]
(h)	Facility services (maintenance, etc.)	[ ]	[ ]	[ ]

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No. — **ITEM DESCRIPTION**

4.3.0 Continued

Service Center	Category Code (1)	Allocation Base Code (2)	Rate Code (3)
(i) Auto pool services	[ ]	[ ]	[ ]
(j) Company aircraft services	[ ]	[ ]	[ ]
(k) Wind tunnels	[ ]	[ ]	[ ]
(l) Other service centers (Enter Code Y on this line if other service centers are used and identify on a continuation sheet each such service center, its Category Code, Allocation Base Code, and Rate Code. If no other service centers are used, enter Code Z.)	[ ]	[ ]	[ ]

4.4.0 Treatment of Variances from Actual Cost (Underabsorption or Overabsorption). Where predetermined billing or costing rates are used to charge costs of service centers to Government contracts or other indirect cost pools (Rate Code A in Column (3) of Item 4.3.0), variances from actual costs are: (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.)

A. ☐ Prorated to users on the basis of charges made, at least once annually

B. ☐ All charged or credited to indirect cost pool(s) at least once annually

Y. ☐ Other(s) (Describe on a continuation sheet.)

Z. ☐ Service center is not applicable to reporting unit

4.5.0 Major Types of Indirect Costs. (For each pool coded other than Z in Items 4.1.0, 4.2.0, and 4.3.0, list on a continuation sheet the major functions, activities, and elements of cost included.)

4.6.0 Allocation Base. (For each allocation base code used in Items 4.1.0, 4.2.0 and 4.3.0, describe on a continuation sheet the makeup of the base; for example, if direct labor dollars is used, are overtime premium, fringe benefits, etc., included?)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No.	ITEM DESCRIPTION

4.7.0 Application of Overhead and G&A Rates to Specified Transactions or Costs.

This item is directed to ascertaining your practice in special situations where, in lieu of establishing a separate indirect cost pool, allocation is made from an established overhead or G&A pool at less than the normal full rate for that pool. The term "less than full rate" below applies to this type of indirect cost allocation practice. The term does not apply to situations where, as in some cases of off-site activities, etc., a separate indirect cost pool and base are used and the rate of such activities is lower than the "in-house" rate.

(For each of the transactions or costs listed below, enter one of the following codes to indicate your indirect cost allocation practice with respect to that transaction or cost. If Code A, Less than full rate, is entered, describe on a continuation sheet the major types of expenses that are covered by such a rate. If Code B, Full rate, is entered, identify on a continuation sheet the pool(s) reported under Items 4.1.0, 4.2.0 and 4.3.0 which are applicable. If Code C, Combination of A and B, is entered, describe on a continuation sheet the applicable expense and pool data.)

Rate Code

A. Less than full rate

B. Full rate

C. Combination of A and B

D. No overhead or G&A is applied

Z. Transaction or cost is not applicable to reporting unit

Transaction or Cost to Which Indirect Costs May Be Allocated	Rate Code
(a) Subcontract costs	[ ]
(b) Purchased labor	[ ]
(c) Government-furnished materials	[ ]
(d) Interorganizational transfers in	[ ]
(e) Interorganizational transfers out	[ ]
(f) Self-constructed depreciable assets	[ ]

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART IV - INDIRECT COSTS

Item No.	ITEM DESCRIPTION

4.7.0 Continued

(g) Labor on installation of assets ☐

(h) Off-site work ☐

(i) Other transactions or costs (Enter Code A on this line if there are other transactions or costs to which less than full rate is applied. List such transactions or costs on a continuation sheet, and for each describe the major types of expenses covered by such a rate. If there are no other such transactions or costs, enter Code Z.) ☐

4.8.0 Independent Research and Development (IR&D) and Bidding and Proposal (B&P) Costs.

4.8.1 Independent Research and Development. IR&D costs are defined in ASPR 15-205.35 or other pertinent procurement regulations, as revised. The full rate of all allocable manufacturing, engineering, and/or other overhead is applied to IR&D costs as if IR&D projects were under contract, and the "burdened" IR&D costs are: (Check one.)

A. ☐ Allocated to Government contracts or similar cost objectives as part of the G&A rate

B. ☐ Allocated as a separate IR&D rate

C. ☐ Transferred to the corporate or home office level. The corporate or home office level IR&D costs are subsequently allocated back to the reporting unit for allocation as part of the unit's G&A rate

D. ☐ Treated the same as C above, except that the IR&D costs are allocated as a separate IR&D rate

Y. ☐ Other (Describe on a continuation sheet.)

Z. ☐ Not applicable

4.8.2 Bidding and Proposal. B&P costs as defined in ASPR 15-205.3 or other pertinent procurement regulations, as revised, are treated as follows: (Check one.)

A. ☐ Same as IR&D costs as checked above

Y. ☐ Other (Describe on a continuation sheet.)

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 91-379

PART V - DEPRECIATION AND CAPITALIZATION PRACTICES

ITEM DESCRIPTION

Depreciating Tangible Assets for Government Contract Costing. (For each of the asset categories listed on Page 22, enter a code from A through G in Column (1) describing the method of depreciation (Code F for assets that are expensed); a code from A through E in Column (2) describing the basis for determining useful life; a code from A through C in Column (3) describing how depreciation methods or use charges are applied to property units; and a Code A, B or C in Column (4) indicating whether or not residual value is deducted from the total cost of depreciable assets. Enter Code Y in each column of an asset category where another or more than one method applies. Enter Code Z in Column (1) only, if an asset category is not applicable.)

Column (1) - Depreciation Method Code

A. Straight-line
B. Declining balance
C. Sum-of-the-years digits
D. Machine hours
E. Unit of production
F. Expensed at acquisition
G. Use charge
Y. Other or more than one method (Describe on a continuation sheet.)
Z. Asset category is not applicable

Column (2) - Useful Life Code

A. U.S. Treasury Department "guideline lives"
B. Replacement experience
C. Term of Lease
D. Engineering estimate
E. As prescribed for use charge by the Office of Management and Budget Circular No. A-21
Y. Other or more than one method (Describe on a continuation sheet.)

Column (3) - Property Units Code

A. Individual units are accounted for separately
B. Applied to groups of assets with similar service lives
C. Applied to groups of assets with varying service lives
Y. Other or more than one method (Describe on a continuation sheet.)

Column (4) - Residual Value Code

A. Residual value is deducted
B. Residual value is covered by the depreciation method (e.g., declining balance)
C. Residual value is not deducted
Y. Other or more than one method (Describe on a continuation sheet.)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES

Item No.	ITEM DESCRIPTION
5.1.0	Continued

	Asset Category	Depreciation Method Code (1)	Useful Life Code (2)	Property Units Code (3)	Residual Value Code (4)
(a)	Land improvements	[ ]	[ ]	[ ]	[ ]
(b)	Building	[ ]	[ ]	[ ]	[ ]
(c)	Building improvements	[ ]	[ ]	[ ]	[ ]
(d)	Leasehold improvements	[ ]	[ ]	[ ]	[ ]
(e)	Machinery and equipment	[ ]	[ ]	[ ]	[ ]
(f)	Furniture and fixtures	[ ]	[ ]	[ ]	[ ]
(g)	Automobiles and trucks	[ ]	[ ]	[ ]	[ ]
(h)	Data processing equipment	[ ]	[ ]	[ ]	[ ]
(i)	Programming/reprogramming costs	[ ]	[ ]	[ ]	[ ]
(j)	Patterns and dies	[ ]	[ ]	[ ]	[ ]
(k)	Tools	[ ]	[ ]	[ ]	[ ]
(l)	Other depreciable asset categories (Enter Code Y on this line if other asset categories are used and enumerate on a continuation sheet each such asset category and the applicable codes. Otherwise enter Code Z.)	[ ]	[ ]	[ ]	[ ]

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES

Item No.	ITEM DESCRIPTION

5.2.0 Depreciation Practices for Costing, Financial Accounting, and Income Tax. Are depreciation practices the same for costing Government contracts as for financial accounting and income tax? (Check one block on each line. Educational institutions and not-for-profit organizations need not complete this item.)

Financial Accounting	A. Yes	B. No
(a) Methods	☐	☐
(b) Useful lives	☐	☐
(c) Property units	☐	☐
(d) Residual values	☐	☐
Income Tax		
(e) Methods	☐	☐
(f) Useful lives	☐	☐
(g) Property units	☐	☐
(h) Residual values	☐	☐

5.3.0 Fully Depreciated Assets. Is a usage charge for fully depreciated assets charged to Government contracts? (Check one. If Yes, describe the basis for the charge on a continuation sheet.)

A. ☐ Yes B. ☐ No Z. ☐ Not applicable

5.4.0 Treatment of Gains and Losses on Disposition of Depreciable Property. Gains and losses are: (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.)

A. ☐ Credited or charged currently to the same overhead or G&A pools to which the depreciation of the assets was charged

B. ☐ Taken into consideration in the depreciation cost basis of the new items, where trade-in is involved

C. ☐ Not accounted for separately, but reflected in the depreciation reserve account

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES

Item No.	ITEM DESCRIPTION

5.4.0 Continued

D. ☐ Credited or charged to Other (Miscellaneous) Income and Expense accounts

Y. ☐ Other(s) (Describe on a continuation sheet.)

Z. ☐ Not applicable

5.5.0 Capitalization or Expensing of Specified Costs. (Check one block on each line to indicate your practices regarding capitalization or expensing of specified costs incurred in connection with capital assets. If the same specified cost is sometimes expensed and sometimes capitalized, check both blocks and describe on a continuation sheet the circumstances when each method is used.)

Cost	A. Expensed	B. Capitalized
(a) Freight-in	☐	☐
(b) Installation costs	☐	☐
(c) Sales taxes	☐	☐
(d) Excise taxes	☐	☐
(e) Architect-engineer fees	☐	☐
(f) Overhauls (extraordinary repairs)	☐	☐
(g) Major modifications or betterments	☐	☐

5.6.0 Criteria for Capitalization. (Enter (a) the minimum dollar amount of expenditures for acquisition, addition, alteration and improvement of depreciable assets, capitalized, and (b) the minimum number of expected life years of capitalized assets. Use leading zeros for dollar amount, e.g., 0150 for $150.

If more than one dollar amount or number applies, show the information for the majority of your depreciable assets, and enumerate on a continuation sheet the dollar amounts and/or number of years for each category or subcategory of assets involved which differ from those for the majority of assets.)

(a) Minimum dollar amount ☐☐☐☐

(b) Minimum life years ☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES

Item No.	ITEM DESCRIPTION
5.7.0	Group or Mass Purchase. Are group or mass purchases (initial complement) of similar items, which individually are less than the capitalization amount indicated above, capitalized? (Check one.) A. [ ] Yes B. [ ] No

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 91-379

PART VI - OTHER COSTS AND CREDITS

Item No.	ITEM DESCRIPTION
6.1.0	Method of Charging and Crediting Vacation, Holiday and Sick Pay. (Check the appropriate block(s) in each column of Items 6.1.1 and 6.1.2 to indicate the method used to charge, or credit any unused or unpaid, vacation, holiday, or sick pay for direct and indirect labor. If more than one method is checked, explain on a continuation sheet.)

		Direct Labor (1)	Indirect Labor (2)
6.1.1	Charges		
	A. When accrued (earned)	☐	☐
	B. When taken	☐	☐
	Y. Other(s) (Describe on a continuation sheet.)	☐	☐
6.1.2	Credits for Unused or Unpaid Vacation, Holiday, or Sick Pay		
	A. Credited to Government contracts at least once annually	☐	☐
	B. Credited to indirect cost pools at least once annually	☐	☐
	C. Credited to Other (Miscellaneous) Income	☐	☐
	D. Not Credited	☐	☐
	Y. Other(s) (Describe on a continuation sheet.)	☐	☐

6.2.0 Supplemental Unemployment (Extended Layoff) Benefit Plans. Costs of such plans are charged to Government contracts: (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.)

A. ☐ When actual payments are made directly to employees

B. ☐ When accrued (book accrual or funds set aside but no trust fund involved)

C. ☐ When contributions are made to a nonforfeitable trust fund

D. ☐ Not charged

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VI - OTHER COSTS AND CREDITS

Item No.	ITEM DESCRIPTION
6.2.0	Continued Y. ☐ Other(s) (Describe on a continuation sheet.) Z. ☐ Not applicable
6.3.0	Severance Pay. Costs of normal turnover severance pay, as defined in ASPR 15-205.39(b)(i) or other pertinent procurement regulations, which are charged directly or indirectly to Government contracts, are based on: (Check the appropriate block(s) and if more than one is checked, explain on a continuation sheet.) A. ☐ Actual payments made B. ☐ Accrued amounts on the basis of past experience C. ☐ Not charged Y. ☐ Other(s) (Describe on a continuation sheet.) Z. ☐ Not applicable
6.4.0	Incidental Receipts. (Check the appropriate block(s) to indicate the method used to account for receipts from renting real and personal property or selling services when related costs have been charged to Government contracts. If more than one is checked, explain on a continuation sheet.) A. ☐ The entire amount of the receipt is credited to the same indirect cost pools to which related costs have been charged B. ☐ The amount of the receipt, less an allowance for profits, is credited to the same indirect cost pools to which related costs have been charged; the profits are credited to Other (Miscellaneous) Income C. ☐ The entire amount of the receipt is credited directly to Other (Miscellareous) Income Y. ☐ Other(s) (Describe on a continuation sheet.) Z. ☐ Not applicable

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VI - OTHER COSTS AND CREDITS

Item No.	ITEM DESCRIPTION

6.5.0 Proceeds from Employee Welfare Activities. Employee welfare activities include all of those activities set forth in ASPR 15-205.10(a) or other pertinent procurement regulations. (Check the appropriate block(s) to indicate the practice followed in accounting for the proceeds from such activities. If more than one is checked, explain on a continuation sheet.)

A. [ ] Proceeds are turned over to an employee-welfare organization or fund; such proceeds are reduced by all applicable costs such as depreciation, heat, light and power

B. [ ] Same as above, except the proceeds are not reduced by all applicable costs

C. [ ] Proceeds are credited at least once annually to the appropriate indirect cost pools to which costs have been charged

D. [ ] Proceeds are credited to Other (Miscellaneous) Income

Y. [ ] Other(s) (Describe on a continuation sheet.)

Z. [ ] Not applicable

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No. | **ITEM DESCRIPTION**

Instructions for Part VII

This part covers pension costs and certain types of deferred incentive compensation and insurance costs. Some organizations may record all of these costs at the corporate or home office level, while others may record them at subordinate organization levels. Still others may record a portion of these costs at the corporate or home office level and the balance at subordinate organization levels. Reporting units, therefore, should obtain the necessary information from the organizational level at which such costs are recorded.

7.1.0 Pension Costs. The actuarial terms used in this item are defined in Opinion Number 8 of the Accounting Principles Board, American Institute of Certified Public Accountants.

7.1.1 Pension Plans Charged to Government Contracts. Does your organization have one or more pension plans whose costs are charged to Government contracts? (Check one.)

A. ☐ Yes (If Yes, list each such plan on a continuation sheet. Indicate the approximate number and type of employees covered by each plan and whether the plan is, or is not, qualified under Internal Revenue Service criteria. Complete Items 7.1.2 through 7.1.9 for the three plans covering the greatest number of employees whose pension costs are charged to Government contracts.)

B. ☐ No (If No, skip to Item 7.2.0.)

7.1.2 Extent of Funding. (Check one block for each plan. In the event the amount funded for each plan is different from the amount charged on the books of account, describe the difference on a continuation sheet.)

	Plan I	Plan II	Plan III
A. Normal costs only	☐	☐	☐
B. Normal costs plus interest on past or prior service costs	☐	☐	☐
C. Normal costs plus an amortized portion of past or prior service costs	☐	☐	☐
Y. Other (Describe on a continuation sheet.)	☐	☐	☐
Z. Not applicable	☐	☐	☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION

7.1.3 Actuarial Cost Method. (Check one block for each plan to show the method used to compute normal and past or prior service costs.)

	Plan I	Plan II	Plan III
A. Accrued benefit cost	☐	☐	☐
B. Aggregate	☐	☐	☐
C. Attained age--initial liability frozen	☐	☐	☐
D. Attained age--initial liability not frozen	☐	☐	☐
E. Entry age--initial liability frozen	☐	☐	☐
F. Entry age--initial liability not frozen	☐	☐	☐
G. Individual level premium	☐	☐	☐
Y. Other (Describe on a continuation sheet.)	☐	☐	☐
Z. Not applicable	☐	☐	☐

7.1.4 Frequency of Actuarial Reevaluations. (Check one block for each plan.)

	Plan I	Plan II	Plan III
A. Annually	☐	☐	☐
B. 2 - 3 years	☐	☐	☐
C. 4 - 5 years	☐	☐	☐
Y. Other (Describe on a continuation sheet.)	☐	☐	☐
Z. Not applicable	☐	☐	☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION

7.1.5 Criteria for Changing Actuarial Computations and Assumptions. (Describe on a continuation sheet your criteria for determining when actuarial assumptions and computations for your funded plan(s) are changed.)

7.1.6 Amortization of Past or Prior Service Costs. (Check one block for each plan to show the period over which past or prior service costs are amortized.)

	Plan I	Plan II	Plan III
A. 10 years or less	☐	☐	☐
B. 11 - 20 years	☐	☐	☐
C. 21 - 40 years	☐	☐	☐
Y. More than one amortization schedule (Describe on a continuation sheet.)	☐	☐	☐
Z. Not applicable	☐	☐	☐

7.1.7 Adjustment for Actuarial Gains and Losses. (Check one block for each plan to show the period for which costs are adjusted for actuarial gains and losses. If actuarial losses for a plan are treated differently from actuarial gains, describe the difference on a continuation sheet.)

	Plan I	Plan II	Plan III
A. Adjustment of past service costs	☐	☐	☐
B. Adjustment of current year's costs	☐	☐	☐
C. Adjustment of future years' costs	☐	☐	☐
Y. Other (Describe on a continuation sheet.)	☐	☐	☐
Z. Not applicable	☐	☐	☐

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION

7.1.8 Unrealized Gains and Losses. Do the actuarial gains and losses reported in Item 7.1.7 above include unrealized gains and losses? (Check one block for each plan. If Yes is checked, describe the method of recognition of such gains and losses on a continuation sheet.)

	Plan I	Plan II	Plan III
A. Yes	☐	☐	☐
B. No	☐	☐	☐
Z. Not applicable	☐	☐	☐

7.1.9 Amortization of Actuarial Gains and Losses. (Check one block for each plan to show the period over which actuarial gains and losses are amortized. If the amortization of actuarial losses for a plan is treated differently from the amortization of actuarial gains, describe the difference on a continuation sheet.)

	Plan I	Plan II	Plan III
A: 10 years or less	☐	☐	☐
B. 11 - 20 years	☐	☐	☐
C. More than 20 years	☐	☐	☐
Y. Other (Describe on a continuation sheet.)	☐	☐	☐
Z. Not applicable	☐	☐	☐

7.2.0 Deferred Incentive Compensation Charged to Government Contracts.

7.2.1 Deferred Incentive Compensation. Does your organization award deferred incentive compensation (i.e., profit sharing, stock bonus, etc.) which is charged to Government contracts? (Check one.)

A. ☐ Yes (If Yes is checked, list each plan by name or title on a continuation sheet and show the approximate number and type of employees covered. Complete Items 7.2.2 and 7.2.3 for the three plans covering the greatest number of employees whose deferred incentive compensation cost is charged to Government contracts.)

B. ☐ No (If No is checked, skip to Item 7.3.0.)

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION

7.2.2 Qualification of Plan. (Check one block for each plan.)

	Plan I	Plan II	Plan III
A. Qualifies under section 401(a) of the Internal Revenue Code of 1954, as amended	☐	☐	☐
B. Does not qualify under section 401(a) of the Internal Revenue Code of 1954, as amended	☐	☐	☐

7.2.3 Method of Charging Costs to Government Contracts. (Check one block for each plan.)

	Plan I	Plan II	Plan III
A. When accrued	☐	☐	☐
B. When contributions are made to a trust fund	☐	☐	☐
C. When paid directly to employees	☐	☐	☐
D. When other "nonqualified" payments are made	☐	☐	☐
Y. Other or more than one method (Describe on a continuation sheet.)	☐	☐	☐

7.3.0 Employee Group Insurance Charged to Government Contracts. (Includes coverage for life, hospital, surgical, medical, long-term disability, accident, etc.)

7.3.1 Method of Providing Insurance. (Check one.)

A. ☐ All by purchase

B. ☐ All self-insured (If checked, skip to Item 7.4.0.)

C. ☐ Combination of A and B above (Describe on a continuation sheet.)

Z. ☐ Not applicable (If checked, skip to Item 7.5.0.)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No. — **ITEM DESCRIPTION**

7.3.2 Type of Purchased Insurance Plans. (Check one.)

A. ☐ Retrospective rating (also called experience rating plan or retention plan)

B. ☐ Manually rated

Y. ☐ Other or more than one type (Describe on a continuation sheet.)

7.3.3 Treatment of Earned Refunds and Dividends from Purchased Insurance Plans. Refunds are also called experience rating credits or retroactive rating credits. All earned refunds and dividends allocable to Government contracts: (Check one.)

A. ☐ Are credited directly or indirectly to contracts in the policy year earned, in the same manner as the premiums are charged

B. ☐ Are credited directly or indirectly to contracts in the year received in the same manner as the premiums are charged, not necessarily in the year earned

C. ☐ Which are estimated to be received in the future are accrued each year, as applicable, to currently reflect the net annual cost of the insurance

D. ☐ Or portions thereof are not credited or refunded to the contractor each year and are retained by the carriers as reserves. (If D is checked, describe on a continuation sheet (i) the purposes of the reserves, other than "claims reserves" retained by carriers and (ii) whether such reserves are refundable on call or upon termination of the policies, clauses, or auxiliary agreements which provide for reserve retentions.)

Y. ☐ Other or more than one method (Describe on a continuation sheet.)

7.3.4 Employee Contributions (Contributory Purchased Insurance Plans). (Check one.)

A. ☐ Plans provide that employees contribute fixed amount, employer is responsible for balance

B. ☐ Plans provide for fixed percentage participation by both employer and employee

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PART VII - DEFERRED COMPENSATION
AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION

7.3.4 Continued

Y. [ ] Other or more than one method (Describe on a continuation sheet.)

Z. [ ] Not applicable

7.3.5 Employee Sharing in Refunds and Dividends (Contributory Purchased Insurance Plans). (Check one.)

A. [ ] Employees do not participate in refunds and dividends unless employer's contribution is less than the refunds and dividends

B. [ ] Employees share in refunds and dividends in the same fixed amount or percentage ratio as their contributions to premium costs

C. [ ] Employees do not share in refunds and dividends

Y. [ ] Other or more than one method (Describe on a continuation sheet.)

Z. [ ] Not applicable

7.4.0 Self-Insurance Programs (Employee Group Insurance). Costs of the self-insurance programs are charged to Government contracts: (Check one.)

A. [ ] When accrued (book accrual only)

B. [ ] When contributions are made to a nonforfeitable fund

C. [ ] When contributions are made to a forfeitable fund

D. [ ] When the benefits are paid to employees

E. [ ] When amounts are paid to an employee welfare plan or union

Y. [ ] Other or more than one method (Describe on a continuation sheet.)

Z. [ ] Not applicable

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION

7.5.0 Workmen's Compensation, Liability and Casualty Insurance (Purchased Insurance Only). All allocable earned refunds and dividends under retrospectively rated workmen's compensation and liability insurance policies, and dividends and deposit refunds under casualty insurance policies, are: (Check one.)

A. ☐ Credited directly or indirectly to Government contracts in the year earned

B. ☐ Credited directly or indirectly to Government contracts in the year received, not necessarily in the year earned

C. ☐ Accrued each year, as applicable, to currently reflect the net annual cost of the insurance

D. ☐ Not credited or refunded to the contractor but are retained by the carriers as reserves

Y. ☐ Other or more than one method (Describe on a continuation sheet.)

Z. ☐ Not applicable

7.6.0 Self-Insurance Programs (Workmen's Compensation, Liability and Casualty Insurance)

7.6.1 Workmen's Compensation and Liability. Costs of such self-insurance programs are charged to Government contracts: (Check one.)

A. ☐ When claims are paid or losses are incurred (no provision for reserves)

B. ☐ When provisions for reserves are recorded based on the present value of the liability

C. ☐ When provisions for reserves are recorded based on the full or undiscounted value, as contrasted with present value, of the liability

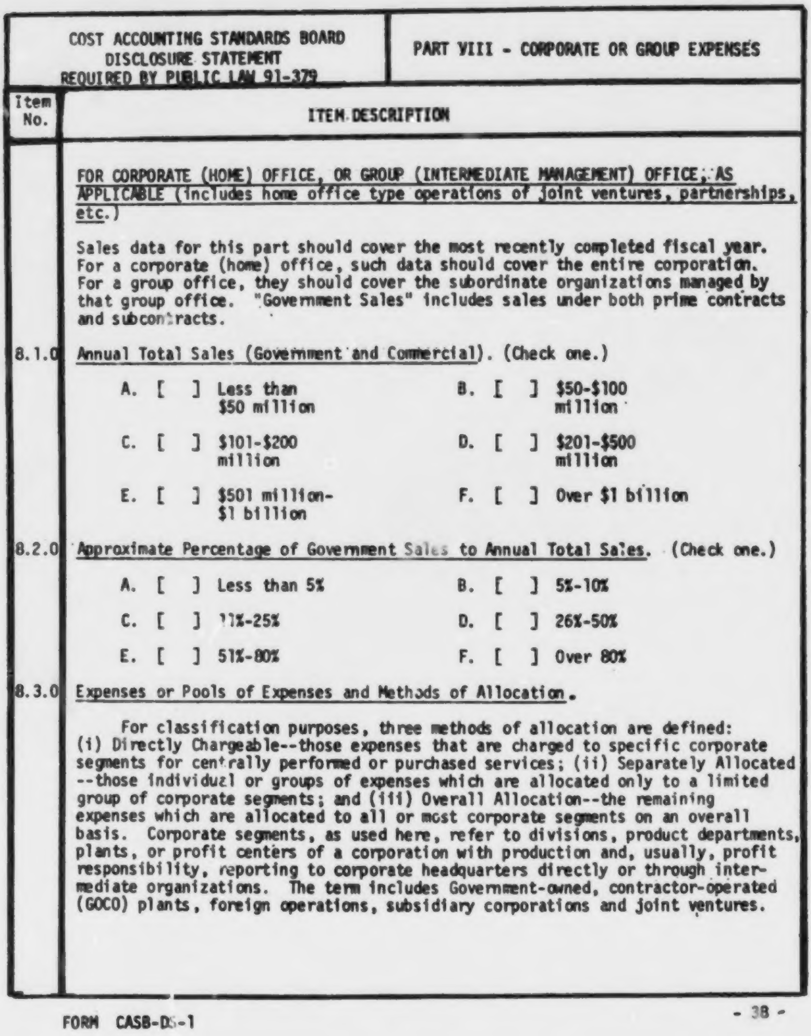
D. ☐ When funds are set aside or contributions are made to a fund

Y. ☐ Other or more than one method (Describe on a continuation sheet.)

Z. ☐ Not applicable

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VII - DEFERRED COMPENSATION AND INSURANCE COSTS

Item No.	ITEM DESCRIPTION
7.6.2	Casualty Insurance. Costs of such self-insurance programs are charged to Government contracts: (Check one.) A. ☐ When losses are incurred (no provision for reserves) B. ☐ When provisions for reserves are recorded based on replacement costs C. ☐ When provisions for reserves are recorded based on reproduction cost new less observed depreciation (market value) excluding the value of land and other indestructibles D. ☐ Losses are charged to retained earnings with no charge to contracts (no provision for reserves) Y. ☐ Other or more than one method (Describe on a continuation sheet.) Z. ☐ Not applicable



COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VIII - CORPORATE OR GROUP EXPENSES

Item No.	ITEM DESCRIPTION

FOR CORPORATE (HOME) OFFICE, OR GROUP (INTERMEDIATE MANAGEMENT) OFFICE, AS APPLICABLE (includes home office type operations of joint ventures, partnerships, etc.)

Sales data for this part should cover the most recently completed fiscal year. For a corporate (home) office, such data should cover the entire corporation. For a group office, they should cover the subordinate organizations managed by that group office. "Government Sales" includes sales under both prime contracts and subcontracts.

8.1.0 Annual Total Sales (Government and Commercial). (Check one.)

A. ☐ Less than $50 million
B. ☐ $50-$100 million
C. ☐ $101-$200 million
D. ☐ $201-$500 million
E. ☐ $501 million-$1 billion
F. ☐ Over $1 billion

8.2.0 Approximate Percentage of Government Sales to Annual Total Sales. (Check one.)

A. ☐ Less than 5%
B. ☐ 5%-10%
C. ☐ 11%-25%
D. ☐ 26%-50%
E. ☐ 51%-80%
F. ☐ Over 80%

8.3.0 Expenses or Pools of Expenses and Methods of Allocation.

For classification purposes, three methods of allocation are defined: (i) Directly Chargeable--those expenses that are charged to specific corporate segments for centrally performed or purchased services; (ii) Separately Allocated--those individual or groups of expenses which are allocated only to a limited group of corporate segments; and (iii) Overall Allocation--the remaining expenses which are allocated to all or most corporate segments on an overall basis. Corporate segments, as used here, refer to divisions, product departments, plants, or profit centers of a corporation with production and, usually, profit responsibility, reporting to corporate headquarters directly or through intermediate organizations. The term includes Government-owned, contractor-operated (GOCO) plants, foreign operations, subsidiary corporations and joint ventures.

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VIII - CORPORATE OR GROUP EXPENSES

Item No. | ITEM DESCRIPTION

Allocation Base Codes

- A. Sales
- B. Cost of sales
- C. Cost input (direct material, direct labor, other direct costs and applicable overhead)
- D. Total cost incurred (cost input plus G&A expenses)
- E. Prime cost (direct material, direct labor, and other direct costs)
- F. Processing or conversion cost (direct labor and applicable overhead)
- G. Direct labor dollars
- H. Direct labor hours
- I. Machine hours
- J. Usage
- K. Unit of product
- L. Direct material cost
- M. Total payroll dollars (direct and indirect employees)
- N. Headcount or number of employees (direct and indirect employees)
- O. Square feet
- Y. Other or more than one basis (Describe on a continuation sheet)

(Enter the type of expenses or the name of the expense pool(s) and one of the Allocation Base Codes A through O, or Y, to indicate the basis of allocation. Use a continuation sheet if additional space is required.)

Item No.	Type of Expenses or Name of Pool of Expenses	Allocation Base Code
8.3.1	Directly Chargeable	
	(a)	[ ]
	(b)	[ ]
	(c)	[ ]
	(d)	[ ]
	(e)	[ ]
8.3.2	Separately Allocated	
	(a)	[ ]
	(b)	[ ]
	(c)	[ ]
	(d)	[ ]
	(e)	[ ]

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	PART VIII - CORPORATE OR GROUP EXPENSES

Item No.	ITEM DESCRIPTION
8.3.3	Overall Allocation (a) [ ] (b) [ ] (c) [ ] (d) [ ] (e) [ ]
8.4.0	Major Types of Expense. (For each pool reported in Items 8.3.1, 8.3.2 and 8.3.3, list on a continuation sheet the major functions, activities, and elements of cost included.)
8.5.0	Allocation Base. (For each Allocation Base used in Items 8.3.2 and 8.3.3, describe on a continuation sheet the makeup of the base; for example, if direct labor dollars is used, are overtime premium, fringe benefits, etc., included?)
8.6.0	Overall Allocation. Are expenses in this category, Item 8.3.3, allocated to all corporate segments? (Check one. If No is checked, list on a continuation sheet the names of excluded corporate segments and the reasons for their exclusion from the allocation.) A. [ ] Yes B. [ ] No
8.7.0	Transfer of Expenses. Are there normally transfers of expenses from corporate segments to corporate or group office? (Check one. If Yes is checked, identify on a continuation sheet the classifications of expense, the names of the corporate segments incurring the expense, and the corporate or group office pools in which the expenses are included.) A. [ ] Yes B. [ ] No
8.8.0	Fixed Management Charges. Are fixed amount of expenses charged to any corporate segments in lieu of a prorata or allocation basis? (Check one. If Yes is checked, list on a continuation sheet the names of such corporate segments and the basis for making fixed management charges.) A. [ ] Yes B. [ ] No
8.9.0	Government Owned/Contractor Operated (GOCO) Plants. Are corporate or group office expenses allocated to GOCO plants? (Check one. If Yes is checked, describe on a continuation sheet the types of expenses involved and the method of allocation.) A. [ ] Yes B. [ ] No Z. [ ] Not applicable

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 91-379	CONTINUATION SHEET Page of Pages
Item No.	ITEM DESCRIPTION

[38 FR 30728, Nov. 7, 1973, as amended at 38 FR 34260, Dec. 12, 1973]

PREAMBLES: For preambles relating to § 351.140, see preambles C and D of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 351.145 Disclosure statement—colleges and universities.

The data which are required to be disclosed by colleges and universities are set forth in detail in the Disclosure Statement Form, CASB-DS-2, which will be devised by the Cost Accounting Standards Board and will be arranged substantially as set forth below.

NOTE: Forms CASB-DS-1 and CASB-DS-2, referred to in 4 CFR 351.140 and 351.145, respectively, when revised, will be modified in accordance with the modifications to 4 CFR 351.130.

[38 FR 34260, Dec. 12, 1973]

PREAMBLE: For preamble relating to § 351.145, see preamble D of the supplement to this part.

APPENDIX A

PRINCIPAL PRODUCT OR SERVICE CODE

(For Item 1.3.0 of the Disclosure Statement)

The following codes and classification descriptions have been selected from the Standard Industrial Classification Manual, 1967, Executive Office of the President (Bureau of the Budget), which is used by U.S. Government agencies to classify establishment data by industry.

For the most part, only those industries which account for a major portion of defense contracting are specifically identified to a significant 4-digit level, that is, a code whose last two digits are each greater than zero. Where the specific industries are not relatively large in defense contracting terms, either a group code (ending in zero) or a major group code (ending in two zeros) is used. An exception to this rule is made when only one specific industry is assignable to a group, e.g., Metal Cases, Code 3411, is used because it is the only industry in Group 3410. One other exception applies to the group code rule: When a specific industry code is used and the group has two or more specific industries, the remaining industry codes within the group are consolidated into a group code ending in zero, e.g., Industrial Gases, is separately identified as Code 2813 and the remaining industries in the group are consolidated into a Group Code 2810 for all other industrial organic and inorganic chemicals.

To obtain the appropriate code for entry in Item 1.3.0 of the Disclosure Statement, each reporting organization should first examine the list of major-group descriptions below to determine which apply to the organization's products or services. Second, the specific codes and descriptions for the major group or groups should be reviewed to select the one code that most nearly identifies the product or service which accounted for most of the organization's sales or shipments in the base fiscal year used for the Disclosure Statement.

If research and development or modification and overhaul is associated with a product, use a specific manufactured product code (Codes 1911 through 3900) rather than a service code. For example, development work associated with aircraft should be coded 3721 (aircraft) rather than 7391 (commercial research and development laboratories).

Following are the major groups whose codes and descriptions are included:

I—Manufactured Products

19 Ordnance and Accessories.
20 Food and Kindred Products.
21 Tobacco Manufactures.
22 Textile Mill Products.
23 Apparel.
24 Lumber and Wood Products except Furniture.
25 Furniture and Fixtures.
26 Paper and Allied Products.
27 Printing, Publishing and Allied Industries.
28 Chemicals and Allied Products.
29 Petroleum Refining.
30 Rubber and Miscellaneous Plastic Products.
31 Leather and Leather Products.
32 Stone, Clay, Glass and Concrete Products.
33 Primary Metal Industries.
34 Fabricated Metal Products, except Ordnance Machinery and Transportation Equipment.
35 Machinery, except Electrical.
36 Electrical Machinery, Equipment and Supplies.
37 Transportation Equipment.
38 Professional, Scientific and Controlling Instruments; Photographic and Optical Goods; Watches and Clocks.
39 Miscellaneous Manufactures.

II—Construction and Services

15 Building Construction.
16 Construction, other than Building Construction.
17 Construction, Special Trade Contractors.
40 Railroad Transportation.

42 Motor Freight Transportation and Warehousing.
44 Water Transportation.
45 Transportation by Air.
47 Transportation Services.
48 Communication.
73 Miscellaneous Business Services.
80 Medical and Other Health Services.
82 Educational Services.

PRINCIPAL PRODUCT OR SERVICE CODE

SECTION I—MANUFACTURED PRODUCTS

Code	Description
	19. ORDNANCE AND ACCESSORIES
1911	*Guns, Howitzers, Mortars, and Related Equipment.* Artillery having a bore over 30 mm, or over 1.18 inches, and components.
1925	*Guided Missiles and Space Vehicles.* Completely assembled guided missiles and space vehicles. Excludes guided missile and space vehicle engines and engine parts (Code 3722); ground and airborne guidance, check-out and launch electronic systems and components (Code 3662); and guided missile and space vehicle airframes, nose cones, and space capsules (Code 3729).
1929	*Ammunition, Except for Small Arms.* Ammunition over 30 mm or 1.18 inches, and also bombs, mines, torpedoes, grenades, depth charges, chemical warfare projectiles, and component parts. Excludes explosives (Code 2892).
1931	*Tanks and Tank Components.* Complete tanks and specialized components for tanks. Excludes military vehicles other than tanks (Code 3711) and tank engines (Code 3519).
1941	*Sighting and Fire Control Equipment.* Includes bomb sights, percentage correctors, wind correctors, directors, and sound locators. Excludes computers and computer systems (Code 3573).
1951	*Small Arms.* Small firearms having a bore 30 mm or 1.18 inches and below, and parts for small firearms. Includes certain weapons over 30 mm which are carried and employed by the individual, such as grenade launchers and heavy field machine guns.
1961	*Small Arms Ammunition.* Ammunition for small arms as defined in Code 1951.
1999	*Ordnance and Accessories, Not Elsewhere Classified.* Examples include flame throwers, Y-guns, and smoke generators.
	20. FOOD AND KINDRED PRODUCTS
2000	Foods and beverages for human consumption, and certain related products, such as manufactured ice, chewing gum, and prepared feeds for animals.
	21. TOBACCO MANUFACTURERS
2100	Cigarettes, cigars, smoking and chewing tobacco, and snuff.

SECTION I—MANUFACTURED PRODUCTS—Continued

Code	Description
	22. TEXTILE MILL PRODUCTS
2200	Includes any of the following: (1) Yarn, thread, braids, twine, and cordage; (2) broad woven fabric, narrow woven fabric, knit fabric, and carpets and rugs from yarn; (3) dyeing and finishing fiber, yarn, fabric and knit apparel; (4) coating, waterproofing, or otherwise treating fabric; (5) the integrated manufacture of knit apparel and other finished articles from yarn; and (6) the manufacture of felt goods, lace goods, bonded-fiber fabrics, and miscellaneous textiles.
	23. APPAREL
2300	Clothing and other finished products fabricated by cutting and sewing purchased or government-furnished textile fabrics and related materials, such as leather, rubberized fabrics, plastics, and furs.
	24. LUMBER AND WOOD PRODUCTS, EXCEPT FURNITURE
2400	Poles, timber and pulpwood, sawmill and planing mill products, flooring, cooperage, millwork, plywood, prefabricated buildings, and wooden containers.
	25. FURNITURE AND FIXTURES
2500	Household, office, public building and restaurant furniture, and office and store fixtures.
	26. PAPER AND ALLIED PRODUCTS
2600	Pulps from rags and from wood and other cellulose fibers; paper and paperboard including building paper and building board, paper bags, boxes, and envelopes.
	27. PRINTING, PUBLISHING AND ALLIED INDUSTRIES
2700	Printing, such as by letterpress, lithography, gravure or screen; bookbinding, typesetting, engraving, and electrotyping; and newspaper, periodical, and book publishing.
	28. CHEMICALS AND ALLIED PRODUCTS
2813	*Industrial Gases.* Gases in compressed liquid, and solid forms. Excludes fluorine and ammonia (Code 2810).
2810	*Industrial Organic, Inorganic Chemicals, Except Industrial Gases.*
2820	*Plastic Materials and Synthetic Resins, Synthetic Rubber, Synthetic and Other Man-Made Fibers, Except Glass Fibers.*
2830	*Drugs and Pharmaceuticals.*
2840	*Soaps, Detergents, and Cleaning Preparations.*
2850	*Paints, Varnishes, Lacquers, and Enamels.*
2860	*Agricultural Chemicals.* Fertilizers and pesticides.
2892	*Explosives.*
2890	*Chemicals, Not Elsewhere Classified.*
	29. PETROLEUM REFINING
2900	Petroleum, paving and roofing materials (asphalt and tar), and lubricating oils and greases.

SECTION I—MANUFACTURED PRODUCTS—Continued

Code	Description
	30. RUBBER AND MISCELLANEOUS PLASTIC PRODUCTS
3000	Products from natural, synthetic or reclaimed rubber; and miscellaneous finished plastic products.
	31. LEATHER AND LEATHER PRODUCTS
3100	Includes finished leather and artificial leather products, and also the tanning, currying, and finishing of hides and skins.
	32. STONE, CLAY, GLASS, AND CONCRETE PRODUCTS
3200	Flat glass and other glass products, cement, structural clay products, pottery, concrete, and gypsum products, cut stone, abrasive and asbestos products.
	33. PRIMARY METAL INDUSTRIES
3310	*Products of Blast Furnaces, Steel Works, and Rolling and Finishing Mills.*
3320	*Iron and Steel Foundry Products.*
3330	*Primary Smelting and Refining of Nonferrous Metals.*
3340	*Secondary Smelting and Refining of Nonferrous Metals.*
3350	*Rolling, Drawing, and Extruding of Nonferrous Metals.*
3360	*Nonferrous Foundry Products.*
3390	*Miscellaneous Primary Metal Products.* Iron, steel, and nonferrous forgings, and primary metal products, not elsewhere classified.
	34. FABRICATED METAL PRODUCTS, EXCEPT ORDNANCE, MACHINERY, AND TRANSPORTATION EQUIPMENT
3411	*Metal cans.*
3420	*Cutlery, Hand Tools and General Hardware.*
3430	*Heating Apparatus (Except Electrical) and Plumbing Fixtures.*
3440	*Fabricated Structural Metal Products.*
3450	*Screw Machine Products and Bolts, Nuts, Screws, Rivets, and Washers.*
3461	*Metal Stampings.*
3470	*Coating, Engraving, and Allied Services.*
3481	*Miscellaneous Fabricated Wire Products.*
3490	*Miscellaneous Fabricated Metal Products.* Barrels, drums, kegs, and pails; safes and vaults; steel springs; valve and pipe fittings, except brass goods and other fabricated metal products, not elsewhere classified.
	35. MACHINERY, EXCEPT ELECTRICAL
3510	*Engines and Turbines.* Steam engines; steam, gas, and hydraulic turbines; steam, gas and hydraulic turbine generator set units; and internal combustion engines not elsewhere classified. Excludes aircraft and rocket engines (Code 3722) and automotive engines (Code 3714).
3522	*Farm Machinery and Equipment.*
3531	*Construction Machinery and Equipment.* Includes heavy machinery and equipment, such as bulldozers, concrete mixers, cranes, dredging machinery, pavers and power shovels.
3532	*Mining Machinery and Equipment.*
3533	*Oil Field Machinery and Equipment.*

SECTION I—MANUFACTURED PRODUCTS—Continued

Code	Description
3534	*Elevators and Moving Stairways.*
3535	*Conveyors and Conveying Equipment.*
3536	*Hoists, Industrial Cranes and Monorail Systems.*
3537	*Industrial Trucks, Tractors, Trailers and Stackers.*
3540	*Metalworking Machinery and Equipment.*
3550	*Special Industry Machinery, Except Metalworking.*
3573	*Electronic Computing Equipment.* Includes general purpose electronic analog computers as well as electronic digital computers. The electronic computers may be used for data processing or may be incorporated as components into control equipment for industrial use, and as components of equipment used in weapons and weapons systems, space and oceanographic exploration, transportation and other systems. Electronic computer systems contain high speed arithmetic and program control units, on-line information storage devices and input/output equipment. Examples of input/output equipment are converters (card and/or tape), readers and printers. Examples of storage devices are magnetic drums and disks, magnetic cores, and magnetic film memories.
3580	*Service Industry Machines.*
3599	*Miscellaneous Machinery, Except Electrical.*
	36. ELECTRICAL MACHINERY, EQUIPMENT AND SUPPLIES
3611	*Electric Measuring Instruments and Test Equipment.* Pocket, portable, panel-board, and graphic recording instruments for measuring electricity, such as voltmeters, ammeters, watt meters, watt-hour meters, demand meters, and other meters and indicating instruments. Also includes analyzers for testing the electrical characteristics of internal combustion engines and radio apparatus.
3612	*Power, Distribution, and Specialty Transformers.* Excludes radio frequency or voice frequency transformers, coils or chokes (Code 3679).
3613	*Switchgear and Switchboard Apparatus.*
3621	*Motors and Generators.* Electric motors (except starting motors) and power generators; motor generators sets; railway motors and control equipment; and motors, generators, and control equipment for gasoline, electric, and oil electric busses and trucks.
3622	*Industrial Controls.* Motor starters and controllers, control accessories, electronic controls and other industrial controls. Excludes automatic temperature controls (Code 3822).
3620	*Electrical Industrial Apparatus, Except Motors and Generators (Code 3621) and Industrial Controls (Code 3622).*
3630	*Household Appliances.*
3640	*Electric Lighting and Wiring Equipment.*
3651	*Radio and Television Receiving Sets, Except Communication Types.* Electronic equipment for home entertainment. Includes public address systems, and music distribution apparatus except records.
3652	*Phonograph Records.*
3661	*Telephone and Telegraph Apparatus.*

SECTION I—MANUFACTURED PRODUCTS—Continued

Code	Description
3662	*Radio and Television Transmitting, Signaling, and Detection Equipment and Apparatus.* Radio and television broadcasting equipment; electric communication equipment and parts, except telephone and telegraph; electronic field detection apparatus, light and heat emission operating apparatus, object detection apparatus and navigational electronic equipment, and aircraft and missile control systems; and high energy particle accelerator systems and equipment designed and sold as a complete package for radiation therapy, irradiation, radiographic inspection, and research (linear accelerators, betatrons, dynamotrons, Vandergraff generators, resonant transformers, insulating core transformers, etc.); high energy particle electronic equipment and accessories sold separately for the construction of linear accelerators, cyclotrons, synchrotrons, and other high energy research installations (transmitters/modulators, accelerating waveguide structures, pulsed electron guns, vacuum systems, cooling systems, etc.); other electric and electronic communication and signaling products, not elsewhere classified. Excludes transmitting tubes (Code 3673).
3671	*Radio and Television Receiving Type Electron Tubes Except Cathode Ray.*
3672	*Cathode Ray Picture Tubes.*
3673	*Transmitting, Industrial, and Special Purpose Electron Tubes.*
3674	*Semiconductors and Related Devices.* Semiconductor and related solid state devices, such as semiconductor diodes and stacks, including rectifiers, integrated microcircuits (semiconductor networks), transistors, solar cells, and light sensitive semiconductor (solid state) devices.
3679	*Electronic Components and Accessories, Not Elsewhere Classified.* Establishments primarily engaged in manufacturing specialty resistors for electronic end products; inductors, transformers, and capacitors and other electronic components, not elsewhere classified.
3690	*Miscellaneous Electrical Machinery, Equipment, and Supplies.* Includes storage and primary batteries, X-ray apparatus, electrical equipment for internal combustion engines and miscellaneous electrical machinery, equipment and supplies, not elsewhere classified.

37. TRANSPORTATION EQUIPMENT

Code	Description
3711	*Motor Vehicles.* Complete passenger automobiles, trucks, commercial cars and buses, and special purpose motor vehicles.
3714	*Motor Vehicle Parts and Accessories.*
3715	*Truck Trailers (Full).*
3721	*Aircraft.* Complete aircraft. Also includes factory type modification and overhaul of aircraft.
3722	*Aircraft Engines and Engine Parts.*
3723	*Aircraft Propellers and Propeller Parts.*
3729	*Aircraft Parts and Auxiliary Equipment, Not Elsewhere Classified.*
3731	*Ship Building and Repairing.* Ships, barges, and lighters, whether propelled by sail or motor power or towed by other craft. Also includes the conversion and alteration of ships.
3732	*Boat Building and Repairing.*

SECTION I—MANUFACTURED PRODUCTS—Continued

Code	Description
3740	*Railroad Equipment.*
3750	*Motorcycles, Bicycles and Parts.*
3790	*Miscellaneous Transportation Equipment.*

38. PROFESSIONAL, SCIENTIFIC, AND CONTROLLING INSTRUMENTS; PHOTOGRAPHIC AND OPTICAL GOODS; WATCHES AND CLOCKS

Code	Description
3811	*Engineering, Laboratory, and Scientific and Research Instruments and Associated Equipment.* Laboratory, scientific, and engineering instruments such as nautical, navigational, aeronautical, surveying, drafting, and instruments for laboratory work and scientific research (except optical instruments Code 3831).
3821	*Mechanical Measuring and Controlling Instruments, Except Automatic Temperature Controls.*
3822	*Automatic Temperature Controls.* Automatic temperature controls activated by pressure, temperature, level, flow, time, or humidity (including pneumatic controls) of the type principally used as components of air conditioning, refrigeration, and comfort heating, or as components of household appliances. Excludes industrial electric controls (Code 3620).
3831	*Optical Instruments and Lenses.* Optical lenses and prisms, and optical instruments such as microscopes, telescopes, field and opera glasses; and optical measuring and testing instruments such as refractometers, spectrometers, spectroscopes, colorimeters, polariscopes.
3840	*Surgical, Medical, and Dental Instruments and Supplies.*
3851	*Ophthalmic Goods.*
3861	*Photographic Equipment and Supplies.* Photographic apparatus, equipment, parts, attachments, and accessories, such as still and motion picture cameras and projection apparatus; photocopy and microfilm equipment blueprinting and diazotype (white printing) apparatus and equipment; and other photographic equipment; and sensitized film, paper, cloth, and plates, and prepared photographic chemicals for use therewith.
3871	*Watches, Clocks, Clockwork Operated Devices, and Parts Except Watchcases.* Clocks (including electric) watches, mechanisms for clockwork operated devices, and clock and watch parts.

39. MISCELLANEOUS MANUFACTURERS

Code	Description
3900	Manufacture of products not classified in any other major manufacturing groups, i.e., from Code 1911 through 3871. Includes jewelry, silverware, musical instruments, toys, sporting and athletic goods and other miscellaneous manufactured products.

SECTION II—CONSTRUCTION AND SERVICES

15. BUILDING CONSTRUCTION—GENERAL CONTRACTORS

Code	Description
1500	Construction of residential, farm, industrial, commercial, public or other buildings.

16. CONSTRUCTION OTHER THAN BUILDING CONSTRUCTION—GENERAL CONTRACTORS

Code	Description
1600	Heavy construction, such as highways and streets, bridges, sewers, railroads, airports, and other types of construction work, except buildings.

17. CONSTRUCTION—SPECIAL TRADE CONTRACTORS

Code	Description
1700	Specialized construction activities, such as plumbing, painting, plastering, carpentering, electrical, etc.

40. RAILROAD TRANSPORTATION

Code	Description
4000	Transportation by line-haul railroad and certain services allied to rail transportation, such as sleeping and dining car services, railway express, and switching and terminal services.

42. MOTOR FREIGHT TRANSPORTATION AND WAREHOUSING

Code	Description
4200	Local or long-distance trucking, transfer, and draying services, or storage of farm products, furniture and other household goods, or commercial goods of any nature. Also includes operation of terminal facilities for handling freight, with or without maintenance facilities.

44. WATER TRANSPORTATION

Code	Description
4463	*Marine Cargo Handling.*—Services directly related to marine cargo handling from the time cargo, for or from a vessel, arrives at shipside, dock, pier, terminal, staging area, or intransit area until cargo loading or unloading operations are completed. Includes the operation and maintenance of piers, docks, and associated buildings and facilities.
4400	*Water Transportation, Except Marine Cargo Handling*—Freight and passenger transportation on the open seas or inland waters, and incidental services such as lighterage, towing, and canal operation. Also includes excursion boats, sightseeing boats, and water taxis.

45. TRANSPORTATION BY AIR

Code	Description
4582	*Airports and Flying Fields*—Operation and maintenance of airports and flying fields and/or the servicing, repairing (except on a factory basis), and storing of aircraft at such airports. Excludes modification and factory type overhaul of aircraft (Code 3721).
4500	*Transportation by Air, Except Airports and Flying Fields.* Domestic and foreign transportation by air and also terminal services.

47. TRANSPORTATION SERVICES

Code	Description
4700	Services incidental to transportation, such as forwarding, packing and crating, and rental of railroad cars.

SECTION II—CONSTRUCTION AND SERVICES—Continued

48. COMMUNICATION

Code	Description
4800	Point-to-point communication service whether by wire or radio, and whether intended to be received aurally or visually; and radio broadcasting and television. Services for the exchange or recording of messages are also included.

73. MISCELLANEOUS BUSINESS SERVICES

Code	Description
7391	*Commercial Research and Development Laboratories.* Research and development activities on a fee or contract basis. Research and development laboratories of companies which manufacture the products developed from their research activities are classified as auxiliary to the manufacturing establishments served.
7392	*Business, Management, Administrative and Consulting Services.* Business and management administrative and consulting services, such as business analyzing business research, efficiency experts, fashion designing and consulting, industrial management, market research, personnel management, public relations counselors, sales engineers, statistical services, tax consultation, and traffic consultants.
7394	*Equipment Rental and Leasing Services.* Includes electronic equipment rental.
7300	Other miscellaneous business services, such as advertising, mailing, stenographic, employment agency, commercial testing and protective services.

80. MEDICAL AND OTHER HEALTH SERVICES

Code	Description
8000	Medical, surgical, and other health service to persons.

82. EDUCATIONAL SERVICES

Code	Description
8221	*Colleges, Universities, and Professional Schools.* Tuition fees at colleges, universities, and professional schools granting academic degrees and requiring for admission at least a high school diploma or equivalent general academic training.
8200	*Other Educational Services.* Excludes services involving colleges, universities, and professional schools and also excludes research and development activities of such institutions (Code 8921).

89. MISCELLANEOUS SERVICES

Code	Description
8911	*Engineering and Architectural Services.* Services of a professional nature in the fields of engineering and architecture.
8921	*Nonprofit Educational and Scientific Research Agencies.* Research at nonprofit establishments including educational institutions.
8900	*Other Miscellaneous Services.*

PREAMBLE A

Preamble to Original Publication, 2-29-72

The material set forth below is the preamble to the original publication of Part 351, February 29, 1972, at 37 FR 4139. For the preambles to the revision of Part 351 (October 4, 1973 and November 7, 1973), see preambles B and C. Portions of this preamble, relating to Parts 331, 400, and 401 have been omitted; they can be found in the supplements to their respective parts. This preamble to the publication of Part 351 is included as part of the administrative history of Part 351.

General comments. The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C. App. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives—improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable representatives or various Government agencies. Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, FEDERAL REGISTER for comment.

To better assure that all who might want to comment had an opportunity to do so, the Board supplemented the FEDERAL REGISTER notice by sending copies of the FEDERAL REGISTER materials directly to about 175 organizations and individuals who had expressed interest or had provided assistance in the development of the published material. Also, a press release was distributed announcing the publication, which resulted in numerous articles in journals. The Board availed itself of all opportunities to publicize the proposals and solicit comments on them.

Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry, associations, public accounting firms, individual companies, and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board's disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

1. *Public availability of disclosure statement.* In a special notice in the notice of proposed rule making, the Board sought comments to assist it in its determination of whether Disclosure Statements submitted by defense contractors and subcontractors should be available to the general public, pursuant to the Public Information Section of the Administrative Procedure Act (5 U.S.C. 552) or whether such information was properly within one of the statutory exceptions to the legal requirement for public availability.

With few exceptions, both Government and industry commentators urged that the Disclosure Statements not be made available to the general public. Numerous arguments were presented. Among them were that public disclosure by a Government official would violate 18 U.S.C. 1905 (a provision in the Criminal Code making it a crime for a Government official to make certain matters public in certain circumstances), thus making disclosure improper under an exception to the requirement for public availability set out in 5 U.S.C. 552(b)(3); that the cost accounting practices were trade secrets or property of considerable value and that disclosure would deprive the company of their value without compensation; that disclosure would reduce competition; and that the public might be misled in that it might construe disclosures respecting the defense segment of a contractor's business as representative of his entire business organization.

An argument in favor of making the Disclosure Statements available to the public was made by a public interest group. It argued that 5 U.S.C. 552 clearly applies to Disclosure Statements, which do not fall within any exception to public availability; that the public requires access to Disclosure Statements in order to consider adequately and comment intelligently on any Cost Accounting Standards proposed by the Board; that public availability would enhance competition; that Disclosure Statements which are ultimately approved will form a body of precedents to guide others in complying with future Board Standards and that public availability will enable citizens and the Congress to hold both the Board and contracting officials accountable for implementation of section 719. A few commentators stated that they favored, or could see no harm to companies from, public availability of contractors' disclosed practices.

The Board is especially impressed with arguments that cost accounting practices have never been made public, that companies have regarded and treated them as confidential, and that a company's competitive position would be damaged by public disclosure of its cost accounting practices. Since disclosure will be required of many companies or divisions of companies whose principal competitors are not subject to Board regulations, the Board recognizes there might arise competitive disadvantage to the disclosing company or division if its competitors may see its disclosure but need make none themselves. The Board has, in light of these latter arguments, concluded that information received in response to Disclosure Statements is within the exception set forth at 5 U.S.C. 552(b)(4) and that the Board will not make Disclosure Statements public in any case when the company or segment files its statement specifically conditioned on the Government's agreement to treat the Disclosure Statement as confidential information.

A provision to this effect has been added at § 351.4(d) of Part 351. Additionally, paragraph (a)(1) of the contract clause set forth at § 331.5 has been modified to this effect, and a provision added to it so that subcontractors may submit Disclosure Statements directly to the contracting officer.

While the Board has concluded that public availability of the Disclosure Statements of identified contractors is not required, it will, nevertheless, implement its announced intention of compiling statistical summaries of disclosure data and making those studies available to the public. The Board believes that the creation of a data bank of cost accounting practices will greatly benefit the Board's own research efforts and the formulation of Cost Accounting Standards; summaries of these data or studies of them should also prove to be of great value to the public. Aggregated information not identified to particular contractors will, therefore, be made available to the public.

2. *Contractor-subcontractor relationships.* Several commentators, stating that contractors cannot dictate the cost accounting practices of their subcontractors at any tier, urged that the Board not hold contractors responsible for increased costs to the United States arising from the failure of subcontractors to follow Cost Accounting Standards or disclosed cost accounting practices. Several commentators also urged that the contractor not be subject to the possibility of a default termination by reason of the actions or inactions of any of its subcontractors at any tier. Finally, some commentators urged that the Board establish a novel concept of privity between the contracting agency and subcontractors with respect to any concerns stemming from Board rules, regulations, and Cost Accounting Standards.

The Board has dealt with many of the issues touched on by these commentators in its conclusions, discussed below, respecting the phasing of applicability and the proposed termination-for-default language in the Contract Clause. The Board is also mindful of the desirability of its maintaining neutrality with respect to contracting policies outside its jurisdiction; thus it should avoid establishing a standard or policy which would influence decisions of whether work should be performed in-house or subcontracted. A Board policy permitting contractors to avoid responsibility for the actions of their subcontractors could surely have such an impact.

The Board reaffirms the established principle that prime contractors are responsible to the Government for performance of their contracts in all required respects and urges that contractors who are fearful of deficiencies in their subcontractors' performances protect themselves by use of whatever means they currently employ under other flow-down contractual requirements.

3. *Exemptions.* Many commentators urged the Board to provide exemptions either to the requirement to file a Disclosure Statement or to both that requirement and the requirement to follow Cost Accounting Standards. Exemptions were urged for subcontractors below the first tier, subcontractors with small amounts of defense contracting business, producers of basic or raw materials, colleges and universities, construction contractors, firms which would qualify as small businesses, and others.

The Board has long been concerned with the question of appropriate exemptions. It has specifically requested interested groups to offer suggestions for criteria for use by the Board in considering exemptions. It also requested its staff to study exemptions and has discussed the staff investigations at Board meetings. In light of these studies and the comments received, the Board has found no persuasive reasons for issuing blanket or class exemptions at this time.

The Board recognizes, however, that individual Cost Accounting Standards may by their nature be inapplicable or inappropriate to certain classes or categories of defense contractors or contracts. The Board will continue to consider exemptions from individual proposed Cost Accounting Standards as appropriate.

With respect to the requirement to submit a Disclosure Statement, the Board's proposed regulation provides a phasing of that requirement. The Board remains convinced that a company which together with its subsidiaries received prime contract awards of negotiated national defense contracts including supplemental awards during Federal fiscal year 1971 totaling more than $30 million should be required to submit a Disclosure Statement as soon as Part 351 of the Board's regulations becomes effective. In order to provide both to other contractors and to Government agencies adequate time within which to study the use of Disclosure Statements, however, the Board will defer determination of the date after which other affected contractors and subcontractors may be required to file Disclosure Statements. From time to time, the Board will announce the dates of applicability to other contractors and subcontractors.

4. *Applicability date of standards, rules, and regulations.* A related issue raised by many commentators is a request that Cost Accounting Standards be made applicable 90 days after issuance or at the beginning of the contractor's next fiscal year, whichever is later. In order to provide the maximum benefits from use of Cost Accounting Standards, the Board has decided not to adopt any rule which would automatically delay the effective date of Cost Accounting Standards beyond the dates contemplated in section 719(h). That section provides a minimum of 4 months' notice from the date of promulgation, to contractors of the likely applicability of a Cost Accounting Standard. The Board regards this as an adequate time for companies to prepare for use of the standard. The Board nevertheless recognizes that certain standards by their nature may require deferring applicability to the beginning of a contractor's fiscal year next following the effective date, and in such cases that applicability will be stated in the standards concerned.

5. *Agency administrative responsibility.* Many commentators, noting the Board's statutory responsibility to promote uniformity and consistency in cost accounting practices used in defense contracting and subcontracting, have suggested that uniformity would be promoted by giving the Board or another single Federal agency the sole implementing responsibility respecting Board regulations. Thus, some commentators recommended that the Board itself issue regulations prescribing the frequency of submission of Disclosure Statements and where they must be submitted. Other commentators urged that the Board issue a single regulation prescribing exact methods by which increased costs to the United States will be determined. Other commentators urged that the Board prescribe methods by which advance agreements affecting more than one contract shall be made, some commentators urging that the Board itself make those agreements. Others urged that the Board rule that the contracting agencies must act to approve or disapprove Disclosure Statements within a stated period of time. And finally, some commentators urged that the Board itself be the sole agency to approve the cost accounting practices disclosed through submission of a Disclosure Statement.

The Board finds these recommendations cogent. It also recognizes that to act pursuant to them would require a Board regulation directed to the administrative and contracting procedures of many Federal agencies and in some cases—such as the recommendation for Board approval of disclosed cost accounting practices—substitute a Board regulation for the exercise of contracting officers' discretion.

The Board, therefore, has decided not to implement at this time the suggestions set forth in this connection. The Board nevertheless will watch closely during the early implementation by contracting agencies of Board rules, regulations, and Cost Accounting Standards so that it may become aware of any diversity of regulations or actions by contracting agencies. If the Board finds that an unacceptable amount of diversity has arisen, it will be prepared to reconsider the recommendations that the Board issue its own regulations in many of the areas left by Board regulations to the discretion of contracting agencies.

Many commentators have expressed concern about the problems which could arise from inconsistent actions by different Federal agencies respecting disclosed practices, changes in practices, and equitable adjustment of contract prices and costs. The Board has directed its staff to work with representatives of relevant Federal agencies with the objective of obtaining designation of a single contracting officer for each contractor or major component thereof in order to achieve consistent practices within the standards issued by the Board.

6. *Contract modifications.* Several commentators have urged that negoti-

ated contract changes and amendments over $100,000 to contracts which are themselves not subject to Board jurisdiction should not be covered. One commentator pointed out that in a long-term contract, most changes represent "instead of" type changes with cost of price adjustments only for the incremental effect of the change. This commentator stated that there is no practical way separately to identify these incremental costs.

The Board is persuaded that for the time being it should not cover negotiated modifications to contracts exempt at their inception. It has, therefore, eliminated coverage for the time being of such contract modifications. In doing so, however, the Board intends that the annual extension of existing negotiated contracts and similar contract modifications would not be exempt from the Board's rules, regulations, and Cost Accounting Standards.

7. *Definitions.* The Board is also persuaded of the value of one commentator's suggestion that the Board provide a compilation of definitions of the words or phrases defined in individual Cost Accounting Standards, making those definitions applicable to all such standards. Consequently, a new Part 400 has been added, and all terms defined in Parts 401 and 402 have been placed in it, although they also remain in the particular standards in which they are defined. As more standards are added, any terms defined in them will also be added to Part 400. However, terms defined in Parts 331 and 351 are not included in the glossary of definitions, nor are terms used in those parts necessarily to bear the meanings ascribed to those terms in Part 400.

8. *Application to individual contracts.* Several commentators urged that the Board adopt the date of final agreement on a negotiated price as a cut-off date for the disclosure of cost accounting practices. The Board has reviewed the merits of selecting that date rather than the date of award to establish the date as of which the contractor's Disclosure Statement must accurately reflect his cost accounting practices, at least with respect to those contracts where cost or pricing data have been submitted pursuant to Pub. L. 87-653. The Board has decided to use the date of final agreement on price, as shown on the signed certificate of current cost or pricing data, with respect to contractors who have submitted cost or pricing data, and to use the date of award of the contract for all other contractors. In addition, the Board has concluded that it is appropriate to use those dates to establish which Cost Accounting Standards shall be applicable to the proposal and to the contract at its inception. Appropriate changes in Parts 331, 351, and 401 have been made to reflect this decision.

9. *Price adjustments.* Many commentators stated that where a contractor's departure from existing disclosed practices is occasioned by the contractor's wish to adopt a newly issued Cost Accounting Standard for all contracts, the Government should be willing to provide upward price adjustment whenever an existing contract is rendered thereby more expensive to perform. The view was often expressed that contractors could not maintain one accounting practice for contracts subject to a particular Cost Accounting Standard, but a different practice for contracts not so subject; therefore, it was alleged, once a contractor had to adopt a standard for any one contract, he would of necessity adopt it for all contracts and amend his Disclosure Statement accordingly.

The Board notes in this connection that the Cost Accounting Standard at Part 402 requires consistency in the allocation of all direct and indirect costs under all covered contracts. If a Cost Accounting Standard were issued which required a company to modify its disclosed cost accounting practices with respect to its earlier practice of allocating direct and indirect costs, Part 402 would require amendment of existing disclosed practices so as to meet that requirement. In such a case, the Board believes it would be unfair to deny an equitable price adjustment arising from such amendment.

Further, the Board has been persuaded by the strong arguments from industry commentators that companies with more than one contract, subject to different Cost Accounting

Standards, cannot maintain multiple records to account for each contract related to its set of standards. Another industry commentator stated that the vast majority of companies must apply any required cost accounting practices across their total business, and that it would be impractical if not impossible for companies to apply different practices to different contracts. The Board has accommodated this view by enabling contractors to apply uniform practices to all covered contracts. Such application will also serve to improve cost accounting practices for all contracts.

The Board has consequently modified both Part 331 and Part 351 to provide three things: First, that a contractor's practices disclosed for any contract shall be the same as the practices currently disclosed and applied on all other covered contracts and subcontracts being performed by that contractor. Second, that a contractor must amend his disclosure of cost accounting practices as new standards are issued and become applicable to new contracts if a change in practices is necessary, so that, at any given time, the same practices prevail under all of the contractor's existing contracts and subcontracts subject to Board jurisdiction. Similarly, contractors must amend Disclosure Statements to reflect any change in practices disclosed under later contracts. Third, that for those amendments of disclosed practices applicable to a particular contract which are occasioned by the issuance of a new Cost Accounting Standard, the Government will equitably adjust the contract price in accordance with the changes clause in the contract or reimburse any increased costs under that contract.

In view of the phasing of the requirement to file a Disclosure Statement, the Board has adopted a contract provision that will provide equitable adjustments in appropriate cases when a contractor who has not yet filed a Disclosure Statement is required to change his established cost accounting practices to comply with newly issued Cost Accounting Standards. On the other hand, any departure from disclosed cost accounting practices which is not required by a newly issued Cost Accounting Standard will not be subject to equitable price adjustment, but only to price adjustment downward in the event that that departure would otherwise result in increased costs being paid by the United States. The Board wishes to emphasize that if the parties to a contractual negotiation mutually agree to a price based on exclusion of costs which are allocable under the contractor's disclosed cost accounting practices, such agreement shall not affect the requirement for conformity with Board rules, regulations, and Cost Accounting Standards in the contractor's allocation of costs between the contract being negotiated and other work.

10. *Materiality.* The Board notes that many commentators urged that a concept of materiality be incorporated in the Board's regulations, to the end that minimal or insignificant modifications of or failures to use disclosed cost accounting practices would not be subject to price adjustment.

The Board agrees that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. Since this rule of common sense is already practiced by the Government, the Board does not believe that there is any need to attempt to formulate and state in acceptable concept of materiality applicable to all Board rules, regulations, and standards, although the Board might consider doing so if subsequent events indicate the necessity therefor. The Board does recognize that in particular standards a "materiality" statement may be useful, and in such cases, it will include one. See for example the addition at § 402.50(e).

11. *Additional requirements by agencies.* As a final general point, concern was expressed that Federal agencies might require submission of cost proposals in ways inconsistent with the cost accounting practices of some or all of the potential offerors. The Board recognizes that this has happened in the past, but it notes that Board rules, regulations, and Cost Accounting Standards are to be used by relevant Federal agencies as well as by contractors and subcontractors, and it believes that henceforth requests for

proposals must be fully consistent with such rules, regulations, and standards, although of course the Federal agency may ask for supplementary information to accompany proposals if this is needed to meet the agency's requirements.

Section 351.14 Disclosure Statement. Several commentators pointed out that the statement was too detailed or complex, or urged that the Statement be modified to require only a statement of cost accounting policy and philosophy. The Board believes that such generalized and unspecific statements would not assist it adequately in performance of its responsibilities. Further, in order to permit the statutory requirements of disclosure of cost accounting practices and consistency to be met, the Board concluded that the extent of detail now called for in the Disclosure Statement is necessary.

Two commentators suggested that references to ASPR, the Internal Revenue Code and financial accounting be deleted from the Disclosure Statement since the contractors stated they are irrelevant to their cost accounting practices. The Board did not agree with these suggestions for the reason that in most cases the regulations have been referred to in the Statement in lieu of redefining certain words, such as "Independent Research and Development Costs." Furthermore, with particular respect to the Internal Revenue Code, the Board cannot ignore that income tax considerations often influence cost accounting practices, such as those for depreciation.

The Board has deleted the item in the Statement calling for an explanation of the difference between commercial and Government cost accounting practices since the Board agrees with several commentators that inclusion of such information in the Disclosure Statement is not needed.

An educational institution and one association pointed out that the terminology in the Disclosure Statement was not responsive to the special circumstances of educational institutions. The Board made appropriate word-changes to a number of items in the Statement to accommodate educational institutions.

By far, the majority of the comments addressed to the Disclosure Statement dealt with suggestions for clarification of terminology and intent of the various items in the statement. The Board considered each comment and made appropriate revisions to the statement. The part most affected by these revisions is Part IV—Indirect Costs. Several items in the part were rearranged in sequence to improve clarity, and instructions covering the items in Part IV were restated.

* * * * *

Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in § 331.8, § 351.4(e), and Parts 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules, or regulations.

* * * * *

3. The provisions of Part 351 will be applicable to any contractor who submits a proposal which results in contracts containing the clause in § 331.5 and whose net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaled more than $30 million. Contractors whose net awards were less than that amount may be required to complete or submit a Disclosure Statement as the Board announced extensions of this requirement to such contractors.

4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this

connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

PREAMBLE B

Preamble to Amendments of 10-4-73

These amendments (38 FR 27507, Oct. 4, 1973) added §§ 351 41 and 351.50(c), and amended § 351.70.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations. A proposed modification to Part 351 was published in the FEDERAL REGISTER of July 27, 1973 (38 FR 20101). That proposal was a revision of an earlier proposal published on May 21, 1973. Thirty-three sets of comments were received in response to the July publication and after considering those comments (discussed below), the Board is today publishing an amendment to its rules relative to the requirement for the submission of Disclosure Statements by defense contractors.

The Board's July 27 proposal required that, in determining who must file Disclosure Statements, only negotiated contracts of the type which are subject to Cost Accounting Standards were to be considered. All commentators who dealt with this matter supported the proposal. The Board, therefore, in the amendments being published today, specifically limits the contract awards to be included in the computation of a contractor's volume of defense contracts in determining whether the revised filing requirement has been met, to those of the type subject to the Board's jurisdiction. The Board recognizes that Standards were not required in contracts in Fiscal Year 1972. In view of this, the amendment refers to "negotiated national defense prime contracts of the type which are subject to Cost Accounting Standards." This filing requirement, therefore, includes all negotiated defense prime contracts in excess of $100,000 except those where the negotiated price is based on (1) established catalog or market prices of commercial items sold in substantial quantities to the general public or (2) prices set by law or regulation, or contracts which are otherwise exempt.

The amendment being published today by the Board to reduce the dollar level above which filing of a Disclosure Statement will be required excludes from the computation the amounts of all subcontracts and those negotiated defense prime contracts not subject to Cost Accounting Standards. In view of this exclusion, the Board is providing that if the dollar volume of prime contract awards to be considered exceeds $10 million, the contractor will be required to submit a Disclosure Statement. Also, in computing the amount, the amendments require that contracts awarded in either Federal Fiscal Year 1972 or 1973 should be considered. Contractors who meet the threshold amount in either year would be required to file Disclosure Statements, effective April 1, 1974.

The Board believes that the inclusion of the amount of subcontract awards in the Disclosure Statement filing requirement would be appropriate because subcontracts, unless specifically exempt, are subject to the Board's Standards, rules and regulations. The Board recognizes, however, that there is a lack of records relative to the nature of subcontracts awarded during fiscal years 1972 and 1973. Because of this, the Board concludes that it is inappropriate to include subcontracts in the determination of the threshold amount for filing Disclosure Statements at this time.

The amendments being published today thus limit consideration to the dollar value of prime contracts only. The Board wishes to point out, however, that future levels of the threshold amount may call for inclusion of the dollar value of subcontract awards in the calculation. Contractors are hereby advised that they may be required to determine the dollar value of negotiated defense subcontract awards subject to Cost Accounting Standards beginning with July 1, 1973. Contractors and subcontractors may find it advantageous to begin to identify and accumulate the value of such awards separately.

A major defense agency commented that reduction of the threshold at this time would be premature. It stated that a large number of Disclosure Statements would now be required from contractors less likely to have sophisticated accounting systems. Consequently, greater agency manpower efforts would be required to review them for adequacy. Also, the agency expressed concern with the upcoming work required for compliance reviews and the possibility of negotiation of price adjustments relative to Standards. Finally, it stated that a number of manpower spaces have already been provided in order to support Board requirements. The agency suggested that a threshold reduction be deferred until after July 1, 1974.

The Board believes that Disclosure Statements from "contractors less likely to have sophisticated accounting systems" would seem to be especially needed by the Government in order to know more precisely how such contractors account for their costs. Additionally, the Government has gained a great deal of experience in reviewing the Disclosure Statements already received, which should aid review of newly submitted statements on an expeditious basis. With respect to the potential workload required in compliance reviews, Government agencies have always had a responsibility for reviewing contractor accounting practices and the use of those practices for Government contract costing. The Disclosure Statement provides a benchmark which should facilitate such reviews in the future. Moreover, the Board is advised that most Disclosure Statements filed under the existing $30 million threshold have been reviewed for adequacy, and compliance reviews are now being made as a part of other routine audit work.

The need to provide manpower spaces to support Board requirements is to be expected. The advantages of the expanded disclosure requirement, however, are many. For example, another defense agency strongly endorsed the Board's proposal to reduce the threshold because of the useful information provided in Disclosure Statements to contracting officers and auditors. Additionally, one agency previously reported to the Board that the Disclosure Statement has become a valuable tool in giving the negotiator more cost visibility while another referred to the Statement as a significant asset for use in reviewing contract proposals. After considering the agencies' comments referred to above, the Board has concluded that a reduction in the threshold is desirable and within the capabilities of the agencies' staffs to review the additional statements that would be submitted.

The Board's July proposal included an effective date of January 1, 1974. The Board has concluded that additional time between the publication of these amendments and the effective date of the reduced threshold should be given to allow agencies to prepare fully to handle the additional volume of Disclosure Statements that will be submitted. Also, additional time will further assure that contractors meeting the new threshold requirement can complete the Disclosure Statement without interference with the prospective award of contracts. For these reasons, the amendments being published today require that contractors meeting the threshold must submit a Disclosure Statement in order to receive a covered contract after April 1, 1974.

Nine commentators urged the Board to provide an exemption for profit centers, divisions, etc., which are predominately commercially oriented and which have only a small dollar volume or percentage of covered defense contracts. The Board has announced that it is initiating a study to consider the establishment of a minimum dollar amount or percentage of covered contract effort below which contractors' profit centers and divisions would be exempt from Board Standards, rules and regulations, including the disclosure requirement. In any case, the Board has concluded that $10 million in covered contracts on a company wide basis is a significant dollar volume and that it warrants establishment of the requirement for submission of a Disclosure Statement.

Two commentators objected to the establishment of an absolute dollar amount of awards as a basis for determining the requirement for filing a Disclosure Statement. They suggested that a percentage of overall business would be more appropriate. This kind of information is not available at the present time. In estimating the number of Disclosure Statements that would be submitted at any threshold amount, and relating that number of statements to the agency's capability to process them, the Board uses statistics on contract awards maintained by defense agencies. Because of this, for the present the Board has retained the requirement to compute the threshold amount for filing a Disclosure Statement in terms of a dollar volume of contract awards. The study discussed above may provide information to allow the Board to consider use of a percentage of covered contracts in relation to total business as a factor in setting future threshold requirements.

While not specifically related to the Board's proposal of July 27, 1973, the Board has received a number of oral inquiries concerning the intent of the second sentence of § 351.120(d) of the Board's regulations, which states:

Revised data for items 1.4.0 through 1.7.0, 8.1.0 and 8.2.0 must be submitted annually at the beginning of the contractor's fiscal year.

The Board did not intend that the changes to these items should be considered in counting the number of changes which would necessitate the resubmission of an entire Disclosure Statement. This information, which relates to the volume of business, should be sent to the recipients of Disclosure Statements only on an annual basis and only if the responses to the items in the Disclosure Statement on file require a change. If on a year-to-year basis, the sales data remain such that the contractor would check the same box in the Disclosure Statement, the Board's rules and regulations do not require resubmission of data concerning these particular items.

The Board's July 27 proposal included a requirement that contractors were to submit a copy of their Disclosure Statement to the Board only after a determination of adequacy has been made of the Statement. All commentators who dealt with this point supported this proposal, and it is included in the amendment being published today.

Today's publication is numbered in consonance with the new numbering system published on September 5, 1973, as part of the proposal set forth in 38 FEDERAL REGISTER 171 at page 23971 et seq. Pending adoption of the September 5, proposal, references to §§ 331.60, 351.40, 351.50, and 351.70 refer to §§ 331.6, 351.4, 351.5 and 351.7 respectively of the Board's current rules and regulations. The new § 351.41 will be located immediately after § 351.4 which will become § 351.40.

PREAMBLE C

Preamble to Revision of Part 351, 11-7-73

This publication (38 FR 30725, Nov. 7, 1973) revised Part 351 in its entirety, with the exception of §§ 351.41, 351.50(c) and the last sentence of § 351.70.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the FEDERAL REGISTER of September 5, 1973 (38 FR 23971). The amendments: (a) Renumber Parts 331 and 351 to facilitate insertion of future modifications to those parts; (b) clarify one section of the contract clause at § 331.5; and (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973:

PREAMBLE D

Preamble to Amendment of 12-12-73

This publication (38 FR 32460, Dec. 12, 1973) amended § 351.140 and added a new § 351.145.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations. A proposed modification to Part 351 was published in the FEDERAL REGISTER of September 17, 1973 (38 FR 26072). That proposal dealt with a Disclosure Statement form designed expressly for submission by colleges and universities. Comments were requested on that proposal from the general public.

Public Law 91-379 which applies to most negotiated defense prime contracts and subcontracts in excess of $100,000 requires that contractors shall disclose in writing their cost accounting practices. The Disclosure Statement form, CASB-DS-1 has been designed to facilitate the meeting of this requirement by contractors. Representatives of colleges and universities had expressed to the Board a desire to have a separate Disclosure Statement to cover their practices. Form CASB-DS-2, being published today, was devised for that purpose and incorporates terminology more commonly used by colleges and universities.

Comments on the September 17 proposal were received from 15 commentators, who offered suggestions for changing the proposed form to explain or further clarify the intent of the questions. Insofar as practicable, the Board has made changes to the college and university Disclosure Statement form to accommodate the suggestions made.

Colleges and universities required to submit Disclosure Statements after April 1, 1974, should use Form CASB-DS-2. Any college or university which has previously submitted a Disclosure Statement should use Form CASB-DS-2 for any amendments which are to be effective after April 1, 1974.

PREAMBLE E

Preamble to Amendments Published 12-24-74

This publication revised §§ 351.40(a) and amended § 351.130, and was published on Dec. 24, 1974, at 39 FR 44389.

The purpose of this publication by the Cost Accounting Standards Board is to adopt modifications to Part 331, Contract Coverage, and Part 351, Basic Requirements, of its rules and regulations. These modifications will provide an exemption from Cost Accounting Standards Board requirements for certain national defense contracts and subcontracts of $500,000 or less.

Public Law 91-379 requires that Cost Accounting Standards must be used in all negotiated prime contract and subcontract national defense procurements with the United States in excess of $100,000, with certain stated exceptions. From time to time the Board refers to contracts subject to its rules and regulations as "covered contracts". Section 719(h)(2) of Pub. L. 91-379 authorizes the Cost Accounting Standard Board to prescribe rules exempting from its requirements such classes or categories of national defense contractors and subcontractors as it determines, on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to be achieved by Pub. L. 91-379. The Board has granted several exemptions to classes or categories of contractors and subcontractors and also has established a procedure under which waiver of the Board's requirements may be granted for individual contracts.

A proposed exemption increasing the minimum contract amount requiring compliance with Cost Accounting Standards Board rules, regulations and Standards from $100,000 to $500,000 was published by the Board on September 27, 1974 (39 FR 34669). The Board received 82 responses to the September 27 proposal. Comments were received from individual companies, government agencies, professional associations, industry associations, public accounting firms, and individuals. All of these comments have been carefully considered by the Board, and the Board takes this opportunity to express its appreciation for the helpful suggestions which have been furnished.

The comments below summarize the major issues discussed by respondents in connection with the initial publication and explain the Board's disposition of these issues.

Issuance of the exemption. Practically all the commentators expressed concurrence in the proposed exemption, giving either unqualified support or support with added comments that additional exemptions should also be considered. However, three commentators—a constituting firm, a major aerospace company and a Government agency—disagreed with the proposed exemption, stating that an increase in the threshold for compliance with CAS requirements was inconsistent with the Board's objective of establishing uniformity and consistency among contractors doing business with the Government.

The Board agrees that the adoption of the proposed regulation will exempt a substantial number of contractors and subcontractors who otherwise would be covered, and consequently will permit such companies to follow accounting practices other than those set out in Cost Accounting Standards. However, the Board is aware that compliance with its rules, regulations and standards may involve additional administrative effort, particularly on the part of small companies, which may not be commensurate with the benefit to the Government or the contractor resulting from such compliance. The Board, after considering the efforts required by both the Government and its contractors to assure compliance on all covered contracts in excess of $100,000, is persuaded that maximum benefit to the Government with minimum cost can be achieved by limiting the mandatory application of its standards to contractors who receive awards which constitute a substantial majority of the national defense procurement dollars. As was stated at the time the proposed exemption was issued for comment, some 70 percent of the prime contractors of the Department of Defense did not receive one or more negotiated awards in excess of $500,000 in Fiscal Year 1973. Thus, only 30 percent, or approximately 750 prime contractors, who received contract awards totaling $20 billion, would continue to be covered. The exemption would remove coverage from only about 10 percent of the dollar value of annual DOD awards.

In view of the foregoing, the Board considers the proposed exemption increasing the minimum contract amount requiring compliance with the Cost Accounting Standards Board rules, regulations, and standards to be in keeping with the purposes sought to be achieved by Pub. L. 91-379 and to be an appropriate exercise of the authority granted to the Board by section 719(h)(2) of that law.

Increase exemption on all contracts to $500,000. A number of commentators suggested that the $500,000 single contract threshold for compliance with Board rules, regulations, and standards be changed to exempt all contracts of $500,000 or less. Those giving reasons in support of this suggestion generally based their comments on simplification of administration. These commentators felt that it would be difficult for the Government or prime contractors, when awarding a prime contract or subcontract in excess of $100,000 to determine whether the contractor or subcontractor had in existence a prior $500,000 covered contract.

The Board, in proposing the $500,000 threshold, did so with the intent of exempting those companies which do not receive contracts in excess of $500,000 from the Government. However, it was decided in the interest of consistency in cost accounting practices that once a contractor had received a covered contract of that size, compliance with CASB rules, regulations and standards on contracts at the level established in Pub. L. 91-379 was appropriate. This is also consistent with the desire expressed by contractors to follow a single set of accounting practices. Further, the requirement for coverage of contracts in excess of $100,000 where the contractor already has received a covered contract in excess of $500,000 will permit the small contracts to be available for equitable adjustment if subsequently issued standards should become applicable. Moreover, once the administrative effort has been expended to comply with standards for contracts in excess of $500,000, compliance with standards on contracts above the statutory threshold of $100,000 requires little added effort.

With respect to the commentators' statements concerning the difficulties, when making an award exceeding $100,000, of determining whether a contractor or subcontractor had in existence a prior award exceeding $500,000 the Board feels that an administrative requirement can be established for obtaining this information. A similar requirement now exists concerning the disclosure statement, whereby contractors are required to submit a disclosure statement, state that they have previously filed a disclosure statement, or submit a certificate of monetary exemption. The Board feels that a similar requirement can be set concerning the $500,000 level. The Board is not persuaded that this matter would create problems of sufficient significance to eliminate coverage down to the $100,000 level.

In considering the advantages of the exemption as proposed compared to its assessment of the administrative difficulties foreseen by commentators, the Board is persuaded that its proposal relative to coverage of awards in excess of $100,000 should not be changed.

Exemption based on sales. A number of commentators urged that the Board establish an exemption based on sales, using either minimum annual dollar amount of sales to the Government, or Government sales as a percentage of total annual sales, or a combination of these two factors. The most frequently suggested amount was $10 million of sales to the Government or Government sales amounting to 10 percent of total annual sales. The objective sought by these commentators was an exemption of those companies or business units whose sales to the Government constituted a reasonably small portion of their total annual sales and whose business was essentially commercially oriented.

The Board has given lengthy consideration to the use of a sales basis for the establishment of a minimum threshold for compliance with its rules, regulations and standards. It did not use that basis at this time due to the nature of the problems involved in administering an exemption based on sales. In either of the situations suggested by commentators, the representation concerning the amount of sales must be made by the contractor and subsequently verified by the Government. This verification would impose very substantial and time-consuming efforts on both the Government and the contractor. Particularly in the case of Government sales as a percentage of total sales, Government representatives would be placed in the position of examining a contractor's total sales, including those made in its commercial business. Examination of a company's records concerning its total sales is not presently performed by Government procurement activities and would present new and unique problems to both parties as well as requiring substantial additional effort on the part of Government representatives.

An exemption based on sales would require a measurement period during which a contractor's status with respect to compliance with standards would be determined. Contracts under which sales were recorded during this period would not be subject to standards. If the volume of sales during the measurement period exceeded a stated threshold, a contractor would then be required to comply with standards under contracts received in subsequent periods. Thus, the contracts that brought the contractor under the Board's rules would not be subject to standards, while those received at a later time would be.

The Board has decided that the administrative problems involved with an exemption based on sales should be considered before establishing such a threshold. The Board will continue to study these problems and investigate whether exemptions based on criteria other than a minimum contract amount would be appropriate and consistent with the purposes of Pub. L. 91-379.

Retroactivity. Several commentators requested that the Board modify its proposal so as to provide retroactive exemption to existing contracts where the circumstances are such that these existing contracts would have been exempt if awarded after the effective date of the proposed regulation.

The Board has no authority to modify existing contractual agreements between the government procurement agencies and their contractors. However, the Board sees nothing inconsistent with its regulations or with Pub. L. 91-379 in modification by the procurement agencies of contracts in this category, assuming of course that the Government receives adequate consideration for deletion of the CAS requirement.

Increase minimum amount. A number of commentators recommended that the exemption proposed be increased to an amount greater than $500,000, the figure of $1,000,000 being frequently mentioned. The Board is not now prepared to raise further the minimum contract amount requiring compliance with its promulgations. The Board, in studying an exemption based on minimum contract amount, concluded that the $500,000 threshold was the most appropriate one for achieving its objectives, all factors considered. The Board will continue to examine various limitations but considers that the threshold established in the proposed exemption best meets its requirements and obligations at this time.

Effect of final payment under contracts subject to CAS clause. Several commentators urged that the exemption of contracts of $500,000 or less should not be dependent on the final payment on contracts which are subject to Board requirements, on the grounds that final payment can occur a substantial period of time after completion of work on a contract and that there are many technicalities in closing out a contract which do not involve cost accounting applications.

The Board considers this point to be well taken and has changed the requirement in § 331.30(b)(8) where it first appears to "notification of final acceptance of all items or work to be delivered." At that time it is considered that all direct costs will have been charged to the contract since all work will have been completed, and any further accounting transactions would be the result of adjustments not directly related to contract performance.

Reduction of contract price by exclusion of commercial items. Some commentators, in reading the introductory comments to the Board's initial publication of this exemption, interpreted the phrase "minimum contract amount requiring compliance" in a manner not at all intended by the Board. These commentators interpreted this phrase to permit the price of a contract subject to standards to be reduced by the value of those individual contract items or subassemblies of final contract items whose prices could be considered to be "catalog" or "market" prices, if sold separately. They requested that the regulation be clarified to reflect their interpretation of the Board's introductory comments.

Those requesting this clarification misunderstood the Board's intentions. The Board does not intend that the price of a contract be adjusted to exclude the price of items or subassemblies which, if purchased separately, might be exempt from the Board's promulgations. Consequently, the change in the regulation requested by commentators on this point would be completely inappropriate.

Definition of contractor. One commentator noted that the prefatory comments to the Board's September 27, 1974, publication specifically mentioned the fact that receipt of a contract in excess of $500,000 by one business unit of a multi-unit company would not in itself require other units of the same company to follow Board requirements. This commentator requested that the definitions of "defense contractor" and "defense subcontractor" contained in § 331.20 (b) and (c) be modified to reflect this intention by the Board.

As the Board stated in its September 27 publication, its contract requirements have been applied to business units, such as a profit center, division, subsidiary, or similar unit of a company, which perform the contract, even in those cases where the contract was entered into on behalf of the overall company rather than the business unit. This application of the Board's requirements to a performing business unit is well established and unchallenged, and clarification of the definitions of "contractor" and "subcontractor" does not appear necessary.

Effective date. Several commentators raised questions concerning the effective date of the eligibility for this exemption in relation to awards received prior to January 1, 1975. Contractors who have received a prime contract or subcontract in excess of $500,000 subject to cost accounting standards prior to January 1, 1975, and on which notification of final acceptance of all items or work to be delivered on that contract or subcontract has not been received, is a contractor who has "already received a contract or subcontract in excess of $500,000," as that phrase is used in § 331.30(b)(8). Therefore, today's publication requires that a contractor meeting this test will be required to comply with standards on all covered prime contracts or subcontracts in excess of $100,000 received after January 1, 1975, under the provisions of § 331.30.

PREAMBLE F

Preamble to Amendments of 8-4-75

This publication (40 FR 32747, Aug. 4, 1975) amended § 351.40 by revising (c) and adding (f); deleted § 351.41; amended § 351.50 by revising (a) and (c) and adding (d); and amended § 351.120 by revising (d) and adding (e). A correction to the language which amended § 351.40 appeared at 40 FR 33819, Aug. 12, 1975.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations and Part 403, Allocation of Home Office Expenses to Segments. A proposed modification to Part 351 was published in the FEDERAL REGISTER of April 3, 1975 (40 FR 14942). Twenty-seven sets of comments were received in response to that publication. After considering those comments, the most significant of which are discussed below, the Board is today publishing an amendment to its rules relative to the requirement for the submission of Disclosure Statements by defense contractors and subcontractors.

1. *Fiscal Year Coverage.* The Board's April 3 proposal provided that any company which, together with its subsidiaries, received more than $10 million in prime contracts subject to Cost Accounting Standards in Government fiscal years 1974 or 1975 would be required to file Disclosure Statements. Board regulations now require the filing of Disclosure Statements on the basis of prime contracts awarded in fiscal years 1971, 1972 or 1973. There were no objections voiced by commentators to the inclusion of fiscal years 1974 and 1975 in the filing requirement. Accordingly, the amendments being published today require that companies who exceeded the threshold amounts in either of those fiscal years will be required to file Disclosure Statements.

2. *Effective Date.* The Board's proposal established July 1, 1975, as the effective date for the requirement to include awards made in fiscal years 1974 and 1975. Most commentators pointed out that in view of the short time permitted between submission of comments on the proposal and the July 1 date, any company which met the new requirement would not have sufficient time to file a satisfactory Disclosure Statement to permit receipt of a covered contract. The Board agrees, and accordingly, the amendments being published today establish an effective date of January 1, 1976, for the new requirement. Thus, any company which, together with its subsidiaries, received more than $10 million in prime contract awards subject to Cost Accounting Standards in Government fiscal years 1974 or 1975 must submit a Disclosure Statement in order to receive a covered national defense contract after January 1, 1976.

The April 3 proposal also provided for including subcontract awards in the computation to determine if a company meets the requirement for the filing of Disclosure Statements, beginning with Federal fiscal year 1976. The proposal stated that companies which met the threshold in fiscal year 1976 would be required to file Disclosure Statements as of July 1, 1976. In view of the need for a company to determine whether or not it met the filing requirement and then have sufficient time in which to prepare a satisfactory Disclosure Statement, the effective date for filing a Disclosure Statement on the basis of fiscal year 1976 data has been changed to March 31, 1977. For fiscal years subsequent to 1976, companies will be required to file

Disclosure Statements as a condition of receiving a contract by March 31 following the end of the fiscal year in which the threshold is met. This should permit contractors to make their eligibility determination in sufficient time to allow preparation of acceptable Disclosure Statements.

3. *Inclusion of Subcontracts.* The Board's proposal required that beginning with Federal fiscal year 1976 (July 1, 1975-June 30, 1976) companies would be required to include, in addition to prime contract awards, the value of subcontract awards received subject to Cost Accounting Standards in their computation to determine if they must file Disclosure Statements. Beginning with that fiscal year and for all subsequent fiscal years, the Board's proposal stated that any company which, together with its subsidiaries, received more than $10 million in prime contract awards and subcontract awards subject to Cost Accounting Standards would be required to file Disclosure Statements.

Some commentators questioned how the value of awards was to be considered in determining if a company met the threshold. The $10 million figure is to include both prime contract awards and subcontract awards and may, in fact, be met by companies receiving only subcontracts subject to Standards. There was no intention that companies must have received one or more prime contracts in order to be required to file a Disclosure Statement. The determination of whether or not a company has $10 million in awards subject to Cost Accounting Standards must include both prime contracts and subcontracts.

A number of commentators objected to the inclusion of subcontract awards in a requirement for filing Disclosure Statements. They argued that in many cases they do not have sufficient information to determine whether a subcontract is subject to Standards. Some commentators stated that in many cases prime contractors pass through to subcontractors all Standard Government contract clauses whether or not they are required to be included in the subcontract. They allege that, in some cases, when the prime contractors are contacted to determine specifically whether or not a subcontract which contains the Cost Accounting Standards Clause is, in fact, subject to Standards, the prime contractor states that it is not. Because of this, the commentators claim they would be required to establish an elaborate information-gathering system to assure that they properly identify every subcontract subject to Standards.

The argument about the adequacy of information concerning coverage of subcontracts has been made to the Board on a number of occasions. In October 1973, when the Board published an earlier revision to the Disclosure Statement filing requirement, it advised contractors that they may be required to determine the dollar value of defense subcontract awards subject to CAS, and encouraged them to begin to identify and accumulate the value of subcontract awards separately. Many contractors are in fact effectively identifying subcontracts subject to Standards. These facts persuade the Board that identification of covered subcontracts is feasible, although the Board recognizes that some firms may have to clarify their information exchange procedures with the prime contractors with whom they do business.

The Board believes that the inclusion of the amount of subcontract awards in the Disclosure Statement filing requirement is appropriate because subcontracts, unless specifically exempt, are legally subject to the Board's Standards, rules and regulations. Accordingly, the amendments being published today provide for the inclusion of subcontract awards subject to Standards in the determination made by a company as to whether or not it must file a Disclosure Statement. This requirement is effective with Government fiscal year 1976 and applies to all subsequent fiscal years.

4. *Change in Fiscal Year Period.* Several commentators noted that the Federal Government is changing the dates of its fiscal year following Federal fiscal year 1976. The new fiscal year period will be from October 1 through the following September 30. The period July 1, 1976, thru September 30, 1976, will be known as Federal fiscal period 197T. These commenta-

tors asked whether or not contracts awarded in that period should be included in some way with a normal fiscal year's contract awards. The Board feels that it is not desirable to upset the regular twelve-month fiscal year computation period and accordingly has concluded that contracts awarded in that three-month period need not be included by companies in determining the value of contract awards received in fiscal year 1976 or any subsequent fiscal year.

5. *Previously Announced Filing Requirements.* The Board's proposal included a requirement that any company which has submitted or was required to submit a Disclosure Statement to the Government under the previously announced filing requirements by virtue of having received a covered contract shall remain subject to those requirements so long as it has any contract subject to Cost Accounting Standards. The proposal also required that Disclosure Statements from those companies on file with the Government must be maintained in current form by those companies. There were virtually no comments received on this requirement. The amendments being published today contain that requirement as set out in the April 3 proposal.

6. *Applicability of CAS 403.* A number of commentators noted that the April 3 proposal deleted § 351.41 of the Board's regulations. This paragraph restated the requirement that only companies that met the Disclosure Statement filing requirement for Federal fiscal year 1971 were required to comply with CAS 403. *Allocation of Home Office Expenses to Segments.* These commentators asked that the Board's position be clarified as to whether or not any current revision to the Disclosure Statement requirement also changed the coverage of CAS 403. It was not the Board's intention to broaden the coverage of CAS 403 at this time. The possibility of extending the coverage of that Standard is the subject of a separate study currently underway. To make the Board's intention wholly clear, § 403.70 of CAS 403 is being revised to state explicitly rather than by cross reference the continuing coverage of that Standard. This revision has no substantive significance whatever, but instead merely sets out specifically what was and continues to be the exemption from that Standard, which was before today accomplished by reference to § 351.40 of the Board's Basic Requirements. Contractors and subcontractors which together with their subsidiaries did not receive net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaling more than $30 million continue to be exempt from Standard 403.

7. *Amendments to Disclosure Statements.* The Board's April 3 proposal also included revised procedures for handling changes to the Disclosure Statement. Contractors would be required to submit only the Disclosure Statement pages on which changes have been made. All commentators supported these revised procedures, and they are being published today as part of the Board's regulations.

The Board's April 3 proposal also included a provision enabling procurement agencies to issue regulations prescribing criteria under which a contractor may be required to submit a complete, updated Disclosure Statement. A number of commentators expressed concern over this provision. They felt that procuring agencies perhaps would issue regulations that were not consistent with the Board's intention and for this reason they urged that the Board prescribe criteria under which procurement agencies could make such a request.

The Board appreciates the concern expressed by the commentators. It would appear, however, that agencies would have a need for a complete, updated Disclosure Statement only where the number of amended pages submitted is so great that review of a Disclosure Statement would obviously be an excessively cumbersome process. The Board urges agencies to consider these views when adopting their criteria for submittal of a complete, updated Disclosure Statement. The Board has concluded that it should not itself set criteria for this particular requirement.

8. *Computation of Dollar Amount of Contract Awards.* A number of commentators asked that the Board clari-

fy its intent as to which contracts should be included in the computation of the dollar amounts. The Board feels that covered contracts awarded in any fiscal year in which the computation is being made should be included. This would mean that for all of fiscal year 1974, negotiated defense prime contracts in excess of $100,000 would be included by a company in determining if it met the requirement to file a Disclosure Statement.

For the first six months of fiscal year 1975 all covered contracts in excess of $100,000 would be included in the figure for that fiscal year. For the balance of fiscal year 1975 only those awards which are subject to Standards would be included. This means that if a company was not performing under a covered contract exceeding $500,000 at January 1, 1975, and did not receive an award exceeding that amount in the last six months of the fiscal year, then only the covered contracts received in the first six months would be included. Only those companies which received an award of $500,000 or more in the last six months of the year would add up their covered contracts, including those subsequently awarded in amounts of $100,000 or more, to arrive at the total amount awarded in that period, to be added to the total for the first six months.

Beginning with Federal fiscal year 1976 only companies which receive at least one award exceeding $500,000 either as a prime contract or subcontract subject to Standards will be required to include the value of awards received to determine if they must file a Disclosure Statement. In essence, it is the Board's intention that contracts subject to Cost Accounting Standards shall be included in the computation to determine if the filing requirement has been met by a company for fiscal year 1974 and all subsequent fiscal years.

9. *Summary of Disclosure Statement Filing Requirements.* The Board has amended the requirement for filing Disclosure Statements a number of times. As a convenience to those affected by CAS, there follows a tabulation showing these requirements.

Fiscal period	Government contracts to be included in computation	Amount (million)	Effective date
Fiscal year 1971	Net negotiated prime defense contracts	$30	Oct. 1, 1972.
Fiscal years 1972, 1973	Defense prime contracts of the type subject to CAS	10	Jan. 1, 1974.
Fiscal years 1974, 1975	Defense prime contracts subject to CAS	10	Jan. 1, 1976.
Fiscal year 1976	Defense prime contracts and subcontracts subject to CAS	10	Mar. 31, 1977.
Following years	Defense prime contracts and subcontracts subject to CAS	10	Mar. 31 following fiscal year.

10. *Modification.* The modifications being adopted today are limited to those areas in which the Board considers clarification or changes warranted at the present time. From time to time the Board may announce further changes in the criteria for applicability of the disclosure requirement.

The following modifications to Part 351 of the Board's regulations are being made, effective August 1, 1975, in view of the foregoing.

PREAMBLE G

Amendment published 9-12-77

The material set forth below is the preamble to the revision of § 351.40(e) and (f). This preamble was part of a document which also set forth amendments to Parts 331, 332 and 403. The complete preamble appears in the supplement to Part 332.

DISCLOSURE STATEMENT REQUIREMENTS

Many commentators suggested that preparation of a Disclosure Statement was burdensome. They also contended that in the situation where a large commercial contractor receives only a few small contracts containing a Cost Accounting Standards clause the need for a Disclosure Statement appears to be minimal. Some asserted that adoption of the proposal to require a Disclosure Statement for all covered contracts would reduce the number of companies that would accept contracts subject to the Board's Standards, rules and regulations. The Board is persuaded that for the time being Disclosure Statements should not be required for all covered contracts. Accordingly it is not adopting the February 16 proposal. The Board is retaining the existing Disclosure Statement requirement provided in Part 351 except that a business unit will be required to submit a Disclosure Statement if it is a company or a segment of a company which received awards of national defense contracts subject to Cost Accounting Standards in excess of $10 million during its preceding cost accounting period rather than the preceding Federal fiscal year.

REVISIONS TO PART 351

Part 332 and the amendments to Part 331 generally will result in annual determinations being made of a contractor's obligation to follow Standards and to submit Disclosure Statements. The determination will be made on the basis of sales and awards data from the immediately preceding cost accounting period. The requirement to continue to submit a disclosure Statement so long as the contractor has a contract subject to Cost Accounting Standards will no longer apply. Disclosure Statements must be maintained for and applied to only those contracts which were awarded during a cost accounting period in which the contractor met the filing requirements of § 351.40. Sections 351.40 and 351.50 have been revised to reflect this change.

EFFECTIVE DATE

The effective date of the regulations being published today is March 10, 1978. Pub. L. 91-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

SUBCHAPTER F—[RESERVED]

SUBCHAPTER G—COST ACCOUNTING STANDARDS

PART 400—DEFINITIONS

Sec.
400.1 Definitions.
400.2 Effective date.

Editorial Note: Each of these definitions is followed by a bracketed note which tells the number of the section where it first appeared, and the location of the preamble to the document which added it.

§ 400.1 Definitions.

(a) This part defines various terms used in standards promulgated by the Cost Accounting Standards Board. Unless the text of a particular standard demands a different definition or the definition is expressly modified for a particular standard, terms defined herein whenever used in any standard shall have the meanings ascribed to them in this part. For convenience, the definitions of terms which are prominent in an individual standard are reprinted in that standard. The selection or non-selection of a particular definition to be reprinted in an individual standard, however, does not affect the applicability of all definitions in this part to that standard.

Accrued Benefit Cost Method. An actuarial cost method under which units of benefit are assigned to each cost accounting period and are valued as they accrue—that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the acturial liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method.)

[This definition first appeared in § 412.30; for the preamble see preamble A of the supplement to Part 412]

Accumulating Costs. The collecting of cost data in an organized manner, such as through a system of accounts.

[See § 401.30; for preamble, see preamble A of supplement to Part 401]

Actual cash value. The cost of replacing damaged property with other property of like kind and quality in the physical condition of the property immediately prior to the damage.

[See § 416.30; for preamble, see preamble A of supplement to Part 416]

Actual cost. An amount determined on the basis of cost incurred as distinguished from forecasted cost. Includes standard cost properly adjusted for applicable variance.

[See §§ 401.30 and 407.30; for preamble, see preamble B of supplement to Part 401 and preamble A of supplement to Part 407]

Actuarial Assumption. A prediction of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, pension fund earnings, changes in values of pension fund assets.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Actuarial Cost Method. A technique which uses actuarial assumptions to measure the present value of future pension benefits and pension fund administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Actuarial Gain and Loss. The effect on pension cost resulting from differences between actuarial assumptions and actual experience.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Actuarial Liability. Pension cost attributable, under the actuarial cost method in use, to years prior to the date of a particular actuarial valuation. As of such date, the actuarial liability represents the excess of the present value of the future benefits and administrative expenses over the present value of future contributions for the normal cost for all plan participants and beneficiaries. The excess of the actuarial liability over the value of the assets of a pension plan is the Unfunded Actuarial Liability.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Actuarial Valuation. The determination, as of a specified date, of the normal cost, actuarial liability, value of the assets of a pension fund, and other relevant values for the pension plan.

[See § 413.30; for preamble, see preamble A of supplement to Part 413]

Allocate. To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

[See § 402.30; for preamble, see preamble A of supplement to Part 402]

Asset accountability unit. A tangible capital asset which is a component of plant and equipment that is capitalized when acquired or whose replacement is capitalized when the unit is removed, transferred, sold, abandoned, demolished, or otherwise disposed of.

[See § 402.30; for preamble, see preamble A of supplement to Part 404]

Bid and Proposal (B&P) Cost. The cost incurred in preparing, submitting, or supporting any bid or proposal which effort is neither sponsored by a grant, nor required in the performance of a contract.

[See § 420.30; for preamble, see preamble A of supplement to Part 420]

Business Unit. Any segment of an organization, or an entire business organization which is not divided into segments.

[See § 411.30; for preamble, see preamble A of supplement to Part 411]

Category of Material. A particular kind of goods, comprised of identical or interchangeable units, acquired or produced by a contractor, which are intended to be sold, or consumed or used in the performance of either direct or indirect functions.

[See § 411.30; for preamble, see preamble A of supplement to Part 411]

Compensated personal absence. Any absence from work for reasons such as illness, vacation, holidays, jury duty or military training, or personal activities, for which an employer pays compensation directly to an employee in accordance with a plan or custom of the employer.

[See § 408.30; for preamble, see preamble A of supplement to Part 408]

Cost input. The cost, except G&A expenses, which for contract costing purposes is allocable to the production of goods and services during a cost accounting period.

[See § 410.30; for preamble, see preamble A of supplement to Part 410]

Cost objective. A function, organizational subdivision, contract or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

[See § 402.30; for preamble, see preamble A of supplement to Part 402]

Cost of Capital Committed to Facilities. An imputed cost determined by applying a cost of money rate to facilities capital.

[See § 414.30; for preamble, see preamble A of supplement to Part 414]

Deferred Compensation. An award made by an employer to compensate an employee in a future cost accounting period or periods for services rendered in one or more cost accounting periods prior to the date of the receipt of compensation by the employee. This definition shall not include the amount of year end accruals for salaries, wages, or bonuses that are to be paid within a reasonable period of time after the end of a cost accounting period.

[See § 415.30; for preamble, see preamble A of supplement to Part 415]

Defined-Benefit Pension Plan. A pension plan in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Defined-Contribution Pension Plan. A pension plan in which the contributions to be made are established in advance and the benefits are determined thereby.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Direct Cost. Any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or labor. Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives.

[See § 402.30; for preamble, see preamble A of supplement to Part 402]

Directly associated cost. Any cost which is generated solely as a result of the incurrence of another cost, and which would not have been incurred had the other cost not been incurred.

[See § 405.30; for preamble, see preamble A of supplement to Part 405]

Entitlement. An employee's right, whether conditional or unconditional, to receive a determinable amount of compensated personal absence, or pay in lieu thereof.

[See § 408.30; for preamble, see preamble A of supplement to Part 408]

Estimating Costs. The process of forecasting a future result in terms of cost, based upon information available at the time.

[See § 401.30; for preamble, see preamble B of supplement to Part 401]

Expressly unallowable cost. A particular item or type of cost which, under the express provisions of an applicable law, regulation, or contract, is specifically named and stated to be unallowable.

[See § 405.30; for preamble, see preamble A of supplement to Part 405]

Facilities Capital. The net book value of tangible capital assets and of those intangible capital assets that are subject to amortization.

[See § 414.30; for preamble, see preamble A of supplement to Part 414]

Final Cost Objective. A cost objective which has allocated to it both direct and indirect costs, and, in the contractor's accumulation system, is one of the final accumulation points.

[See § 402.30; for preamble, see preamble A of supplement to Part 402]

Fiscal Year. The accounting period for which annual financial statements are regularly prepared, generally a period of 12 months, 52 weeks, or 53 weeks.

[See § 406.30; for preamble, see preamble A of supplement to Part 406]

Funded Pension Cost. The portion of pension costs for a current or prior cost accounting period that has been paid to a funding agency or, under a pay-as-you-go plan, to plan participants or beneficiaries.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Funding Agency. An organization or individual which provides facilities to receive and accumulate assets to be used either for the payment of benefits under a pension plan, or for the purchase of such benefits.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

General and Administrative (G&A) expense. Any management, financial, and other expense which is incurred by or allocated to a business unit and which is for the general management and administration of the business unit as a whole. G&A expense does not include those management expenses whose beneficial or casual relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

[See § 410.30; for preamble, see preamble A of supplement to Part 410]

Home office. An office responsible for directing or managing two or more, but not necessarily all, segments of an organization. It typically establishes policy for, and provides guidance to the segments in their operations. It usually performs management, supervisory, or administrative functions, and may also perform service functions in support of the operations of the various segments. An organization which has intermediate levels, such as groups, may have several home offices which report to a common home office. An intermediate organization may be both a segment and a home office.

[See § 403.30; for preamble, see preamble B of supplement to Part 403]

Immediate-Gain Actuarial Cost Method. Any of the several actuarial cost methods under which actuarial gains and losses are included as part of the unfunded actuarial liability of the pension plan, rather than as part of the normal cost of the plan.

[See § 413.30; for preamble, see preamble A of supplement to Part 413]

Independent Research and Development (IR&D) Cost. The cost of effort which is neither sponsored by a grant, nor required in the performance of a contract, and which falls within any of the following three areas:

(i) Basic and applied research,

(ii) Development, and

(iii) Systems and other concept formulation studies.

[See § 420.30; for preamble, see Preamble A of supplement to Part 420]

Indirect Cost. Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

[See § 402.30; for preamble, see preamble A of supplement to Part 402]

Indirect cost pool. A grouping of incurred costs identified with two or more objectives but not identified specifically with any final cost objective.

[See § 401.30; for preamble, see preamble A of supplement to Part 401]

Insurance administration expenses. The contractor's costs of administering an insurance program, e.g., the costs of operating an insurance or risk-management department, processing claims, actuarial fees, and service fees paid to insurance companies, trustees, or technical consultants.

[See § 416.30; for preamble, see preamble A of supplement to Part 416]

Intangible Capital Asset. An asset that has no physical substance, has more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the benefits it yields.

[See § 414.30; for preamble, see preamble A of supplement to Part 414]

Labor Cost at Standard. A pre-established measure of the labor element of cost, computed by multiplying labor-rate standard by labor-time standard.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Labor-Rate Standard. A pre-established measure, expressed in monetary terms, of the price of labor.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Labor-Time Standard. A pre-established measure, expressed in temporal terms, of the quantity of labor.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Material Cost at Standard. A pre-established measure of the material element of cost, computed by multiplying material-price standard by material-quantity standard.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Material Inventory Record. Any record used for the accumulation of actual or standard costs of a category of material recorded as an asset for subsequent cost allocation to one or more cost objectives.

[See § 411.30; for preamble, see preamble A of supplement to Part 411]

Material-Price Standard. A pre-established measure, expressed in monetary terms, of the price of material.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Material-Quantity Standard. A pre-established measure, expressed in physical terms, of the quantity of material.

[See § 407.30; for preamble, see Preamble A of supplement to Part 407]

Moving Average Cost. An inventory costing method under which an average unit cost is computed after each acquisition by adding the cost of the newly acquired units to the cost of the units of inventory on hand and dividing this figure by the new total number of units.

[See § 411.30; for preamble, see preamble A of supplement to Part 411]

Multiemployer Pension Plan. A plan to which more than one employer contributes and which is maintained pursuant to one or more collective bargaining agreements between an employee organization and more than one employer.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Normal Cost. The annual cost attributable, under the actuarial cost method in use, to years subsequent to a particular valuation date.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Operating revenue. Amounts accrued or charged to customers, clients, and tenants, for the sale of products manufactured or purchased for resale, for services, and for rentals of property held primarily for leasing to others. It includes both reimbursable costs and fees under cost-type contracts and percentage-of-completion sales accruals except that it includes only the fee for management contracts under which the contractor acts essentially as an agent of the Government in the erection or operation of Government-owned facilities. It excludes incidental interest, dividends, royalty, and rental income, and proceeds from the sale of assets used in the business.

[See § 403.30; for preamble, see preamble A of supplement to Part 403]

Original complement of low cost equipment. A group of items acquired for the initial outfitting of a tangible capital asset or an operational unit, or a new addition to either. The items in the group individually cost less than the minimum amount established by the contractor for capitalization for the classes of assets acquired but in the aggregate they represent a material investment. The group, as a complement, is expected to be held for continued service beyond the current period. Initial outfitting of the unit is completed when the unit is ready and available for normal operations.

[See § 408.30; for preamble, see preamble A of supplement to Part 408]

Pay-As-You-Go Cost Method. A method of recognizing pension cost only when benefits are paid to retired employees or their beneficiaries.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Pension Plan. A deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirement: *Provided,* That the benefits are paid for life or are payable for life at the option of the employees. Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees may be an integral part of a pension plan.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Pension Plan Participant. Any employee or former employee of an employer or any member or former member of an employee organization, who is or may become eligible to receive a benefit from a pension plan which covers employees of such employer or member of such organization who have satisfied the plan's participation requirements, or whose beneficiaries are receiving or may be eligible to receive any such benefit. A participant whose employment status with the employer has not been terminated is an active participant of the employer's pension plan.

[See § 413.30; for preamble, see preamble A of supplement to Part 413]

Pricing. The process of establishing the amount or amounts to be paid in return for goods or services.

[See § 401.30; for preamble, see preamble A of supplement to Part 401]

Production Unit. A grouping of activities which either uses homogeneous inputs of direct material and direct labor or yields homogeneous outputs such that costs or statistics related to these homogeneous inputs or outputs are appropriate as bases for allocating variances.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Projected average loss. The estimated long-term average loss per period for periods of comparable exposure to risk of loss.

[See § 416.30; for preamble, see preamble A of supplement to Part 416]

Projected Benefit Cost Method. Any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers.

[See § 412.30; for preamble, see preamble A of supplement to Part 412]

Proposal. Any offer or other submission used as a basis for pricing a contract, contract modification or termination settlement or for securing payments thereunder.

[See § 401.30; for preamble, see preamble A of supplement to Part 401]

Repairs and maintenance. Maintenance is the regularly recurring activity of keeping assets in normal or expected operating condition. Repair is the activity of putting them back into normal or expected operating condition. The total endeavor to obtain the expected service during the life of tangible capital assets is generally called repairs and maintenance.

[See § 404.30; for preamble, see preamble A of supplement to Part 404]

Reporting Costs. Provision of cost information to others. The reporting of costs involves selecting relevant cost data and presenting it in an intelligible manner for use by the recipient.

[See § 401.30; for preamble, see preamble A of supplement to Part 401]

Residual value. The proceeds (less removal and disposal costs, if any, realized upon disposition of a tangible capital asset. It usually is measured by the net proceeds from the sale or other disposition of the asset, or its fair value if the asset is traded in on another asset. The estimated residual value is a current forecast of the residual value.

[See § 409.30; for preamble, see preamble A of supplement to Part 409]

Segment. One of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

[See § 403.30; for preamble, see preamble A of supplement to Part 403]

Self-insurance charge. A cost which represents the projected average loss under a self-insurance plan.

[See § 416.30; for preamble, see preamble A of supplement to Part 416]

Service life. The period of usefulness of a tangible capital asset (or group of assets) to its current owner. The period may be expressed in units of time or output. The estimated service life of a tangible capital asset (or group of assets) is a current forecast of its service life and is the period over which depreciation cost is to be assigned.

[See § 409.30; for preamble, see preamble A of supplement to Part 409]

Spread-Gain Actuarial Cost Method. Any of the several projected benefit actuarial cost methods under which actuarial gains and losses are included as part of the current and future normal costs of the pension plan.

[See § 413.30; for preamble, see preamble A of supplement to Part 413]

Standard Cost. Any cost computed with the use of pre-established measures.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Tangible capital asset. An asset that has physical substance, more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the services it yields.

[See § 404.30; for preamble, see preamble A of supplement to Part 404]

Termination Gain or Loss. An actuarial gain or loss resulting from the difference between the assumed and actual rates at which plan participants separate from employment for reasons other than retirement, disability, or death.

[See § 413.30; for preamble, see preamble A of supplement to Part 413]

Unallowable cost. Any cost which, under the provisions of any pertinent law, regulation, or contract, cannot be included in prices, cost reimbursements, or settlements under a Government contract to which it is allocable.

[See § 405.30; for preamble, see preamble A of supplement to Part 405]

Variance. The difference between a pre-established measure and an actual measure.

[See § 407.30; for preamble, see preamble A of supplement to Part 407]

Weighted Average Cost. An inventory costing method under which an average unit cost is computed periodically by dividing the sum of the cost of beginning inventory plus the cost of acquisitions, by the total number of units included in these two categories.

[See § 411.30; for preamble, see preamble A of supplement to Part 411]

(Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168)

[37 FR 4171, Feb. 29, 1972, as amended at 37 FR 26680, Dec. 14, 1972]

EDITORIAL NOTE: For FR citations affecting § 400.1, see the List of CFR Sections Affected in the Finding Aids section of this volume.

§ 400.2 Effective date.

July 1, 1972.

(Sec. 103, 84 Stat. 796, 50 U.S.C. App. 2168)

[37 FR 9609, May 13, 1972]

PART 401—COST ACCOUNTING STANDARD—CONSISTENCY IN ESTIMATING, ACCUMULATING AND REPORTING COSTS

Sec.

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APPENDIX—INTERPRETATION No. 1
PREAMBLES A—D

AUTHORITY: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

SOURCE: 37 FR 4172, Feb. 29, 1972, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in non-technical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (37 FR 4172, February 29, 1972) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections; see the references following those sections.

§ 401.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

PREAMBLES: For preambles to § 401.10, see preamble D of the supplement to this part.

For preamble to superseded regulations see preamble A of the supplement.

§ 401.20 Purpose.

The purpose of this Cost Accounting Standard is to insure that each contractor's practices used in estimating costs for a proposal are consistent with cost accounting practices used by him in accumulating and reporting costs. Consistency in the application of cost accounting practices is necessary to enhance the likelihood that comparable transactions are treated alike. With respect to individual contracts, the consistent application of cost accounting practices will facilitate the preparation of reliable cost estimates used in pricing a proposal and their comparison with the costs of performance of the resulting contract. Such comparisons provide one important basis for financial control over costs during contract performance and aid in establishing accountability for costs in the manner agreed to by both parties at the time of contracting. The comparisons also provide an improved basis for evaluating estimating capabilities.

§ 401.30 Definitions.

(a) The following definitions of terms which are prominent in this standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Accumulating Costs.* The collecting of cost data in an organized manner, such as through a system of accounts.

(2) *Actual cost.* An amount determined on the basis of cost incurred as distinguished from forecasted cost. Includes standard cost properly adjusted for applicable variance.

(3) *Estimating costs.* The process of forecasting a future result in terms of cost, based upon information available at the time.

(4) *Indirect cost pool.* A grouping of incurred costs identified with two or more objectives but not identified specifically with any final cost objective.

(5) *Pricing.* The process of establishing the amount or amounts to be paid in return for goods or services.

(6) *Proposal.* Any offer or other submission used as a basis for pricing a contract, contract modification or termination settlement or for securing payments thereunder.

(7) *Reporting costs.* Provision of cost information to others.

The reporting of costs involves selecting relevant cost data and presenting it in an intelligible manner for use by the recipient.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this standard: None.

[37 FR 4172, Feb. 29, 1972, as amended at 38 FR 30730, Nov. 7, 1973]

PREAMBLES: For preambles relating to § 401.30, see preambles A and B of the supplement to this part.

§ 401.40 Fundamental requirement.

(a) A contractor's practices used in estimating costs in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs.

(b) A contractor's cost accounting practices used in accumulating and reporting actual costs for a contract shall be consistent with his practices used in estimating costs in pricing the related proposal.

(c) The grouping of homogeneous costs in estimates prepared for proposal purposes shall not per se be deemed an inconsistent application of cost accounting practices under paragraphs (a) and (b) of this section when such costs are accumulated and reported in greater detail on an actual cost basis during contract performance.

§ 401.50 Techniques for application.

(a) The standard allows grouping of homogeneous costs in order to cover those cases where it is not practicable to estimate contract costs by individual cost element or function. However, costs estimated for proposal purposes shall be presented in such a manner and in such detail that any significant cost can be compared with the actual cost accumulated and reported therefor. In any event the cost accounting practices used in estimating costs in pricing a proposal and in accumulating and reporting costs on the resulting contract shall be consistent with respect to:

(1) The classification of elements or functions of cost as direct or indirect; (2) the indirect cost pools to which each element or function of cost is charged or proposed to be charged; and (3) the methods of allocating indirect costs to the contract.

(b) Adherence to the requirement of § 401.40(a) of this standard shall be determined as of the date of award of the contract, unless the contractor has submitted cost or pricing data pursuant to Pub. L. 87-653, in which case adherence to the requirement of § 401.40(a) shall be determined as of the date of final agreement on price, as shown on the signed certificate of current cost or pricing data. Notwithstanding § 401.40(b), changes in established cost accounting practices during contract performance may be made when authorized by standards, rules, and regulations issued by the Cost Accounting Standards Board.

§ 401.60 Illustrations.

(a) The following examples are illustrative of applications of cost accounting practices which are deemed to be consistent.

Practices used in estimating costs for proposals	Practices used in accumulating and reporting costs of contract performance
1. Contractor estimates an average direct labor rate for manufacturing direct labor by labor category or function.	1. Contractor records manufacturing direct labor based on actual cost for each individual and collects such costs by labor category or function
2. Contractor estimates an average cost for minor standard hardware items, including nuts, bolts, washers, etc	2. Contractor records actual cost for minor standard hardware items based upon invoices or material transfer slips.
3. Contractor uses an estimated rate for manufacturing overhead to be applied to an estimated direct labor base. He identifies the items included in his estimate of manufacturing overhead and provides supporting data for the estimated direct labor base.	3. Contractor accounts for manufacturing overhead by individual items of cost which are accumulated in a cost pool allocated to final cost objectives on a direct labor base.

(b) The following examples are illustrative of application of cost accounting practices which are deemed not to be consistent.

Practices used for estimating costs for proposals	Practices used in accumulating and reporting costs of contract performance
4. Contractor estimates a total dollar amount for engineering labor which includes disparate and significant elements or functions of engineering labor. Contractor does not provide supporting data reconciling this amount to the estimates for the same engineering labor cost functions for which he will separately account in contract performance.	4. Contractor accounts for engineering labor by cost function, i.e., drafting, designing, production engineering, etc.
5. Contractor estimates engineering labor by cost function, i.e., drafting, production engineering, etc.	5. Contractor accumulates total engineering labor in one undifferentiated account.
6. Contractor estimates a single dollar amount for machining cost to cover labor, material and overhead.	6. Contractor records separately the actual cost of machining labor and material as direct costs, and factory overhead as indirect costs.

§ 401.70 Exemptions.

None for this standard.

§ 401.80 Effective date.

July 1, 1972.

[37 FR 9609, May 13, 1972]

PREAMBLE: Preamble A of the supplement to this part explains how effective dates are determined.

APPENDIX—INTERPRETATION NO. 1

Part 401, Cost Accounting Standard Consistency in Estimating, Accumulating and Reporting Costs, requires in § 401.40 that a contractor's "practices used in estimating costs in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs."

In estimating the cost of direct material requirements for a contract, it is a common practice to first estimate the cost of the actual quantities to be incorporated in end items. Provisions are then made for additional direct material costs to cover expected material losses such as those which occur, for example, when items are scrapped, fail to meet specifications, are lost, consumed in the manufacturing process, or destroyed in testing and qualification processes. The cost of some or all of such additional direct material requirements is often estimated by the application of one or more percentage factors to the total cost of basic direct material requirements or to some other base.

Questions have arisen as to whether the accumulation of direct material costs in an undifferentiated account where a contractor estimates a significant part of such costs by means of percentage factors is in compliance with Part 401. The most serious questions pertain to such percentage factors which are not supported by the contractor with accounting, statistical, or other relevant data from past experience, nor by a program to accumulate actual costs for comparison with such percentage estimates. In the opinion of the Board the accumulation of direct costs in an undifferentiated account in this circumstance is a cost accounting practice which is not consistent with the practice of estimating a significant part of costs by means of percentage factors. This situation is virtually identical with that described in Illustration § 401.60(b)(5), which deals with labor.

Part 401 does not, however, prescribe the amount of detail required in accumulating and reporting costs. The Board recognizes that the amount of detail required may vary considerably depending on the percentage factors used, the data presented in justification or lack thereof, and the significance of each situation. Accordingly, the Board is of the view that it is neither appropriate nor practical for the Board to prescribe a single set of accounting practices which would be consistent in all situations with the practices of estimating direct material costs by percentage factors. The Board considers, therefore, that the amount of accounting and statistical detail to be required and maintained in accounting for this portion of direct material costs has been and continues to be a matter to be decided by Government procurement authorities on the basis of the individual facts and circumstances.

[41 FR 52428, Nov. 30, 1976]

PREAMBLE: For the preamble relating to Interpretation No. 1, see preamble C of the supplement.

PREAMBLE A

Original Publication of Part 401, 2-29-72

Preamble to the original publication of 4 CFR Part 401, 37 FR 4139, Feb. 29, 1972. Because that publication also added 4 CFR Parts 331, 351, 400, and 402, material relating to those parts has been omitted. It appears in the Supplements to those parts.

General comments. The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C. app. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives—improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable representatives of various Government agencies, Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, FEDERAL REGISTER for comment.

To better assure that all who might want to comment had an opportunity to do so, the Board supplemented the FEDERAL REGISTER notice by sending copies of the FEDERAL REGISTER materials directly to about 175 organizations and individuals who had expressed interest or had provided assistance in the development of the published material. Also, a press release was distributed announcing the publication, which resulted in numerous articles in journals. The Board availed itself of all opportunities to publicize the proposals and solicit comments on them.

Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry associations, public accounting firms, individual companies and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board's disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

* * * * *

Section 401.20 Purpose. Commentators stated that the purpose of the standards would require each contractor to revise his formal system of accounts in order to maintain them on a basis used for estimating Government contracts. The Board did not intend that requirement. The standard does not contain any requirement that a contractor must revise his formal system of accounts. Cost accounting records are supplemental to, and generally subsidiary to a contractor's financial records. However, it is necessary that the cost accounting records be reconcilable to the contractor's general financial records.

Two commentators believed that the term "practices" in the phrase "Practices used in estimating costs in pricing proposals" could be confused as including estimating techniques relating to quantitative determination as well as the cost accounting practices used in estimating. The Board does not agree, because nothing in the standard precludes the use of any quantitative estimating tools.

Section 401.50 Techniques for application. Several commentators believed there may be an inconsistency between the requirements of the standard and the ability to make changes to established cost accounting practices. The Board intends that compliance with respect to proposals shall be determined as of the award date of the contract or as of the date of final agreement on price if the contractor has submitted cost or pricing data pursuant to Pub. L. 87-653. Modifications of established cost accounting practices for accumulating and reporting costs are permitted by other regulations of the Cost Accounting Standards Board without causing a violation of this standard. The Board has modified the standard to express these intentions.

Section 401.60 Illustration. An illustration has been added to this section to emphasize a requirement of the standard that any significant cost must be accumulated and reported in sufficient detail to permit its comparison with the estimates made therefor.

* * * * *

Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in § 331.8, § 351.4(e), and Parts 400. 401. and 402. which were transmitted to the Congress on February 24. 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules, or regulations.

* * * * *

4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

PREAMBLE B

Preamble to Amendments of 11-7-73

Preamble to revision of the definitions of "actual cost" and "indirect cost pool" in § 401.30(a)(2) and (4), published at 38 FR 30725, Nov. 7, 1973. Material referring to other parts of 4 CFR Chapter III has been omitted; it appears in the Supplements to those parts.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331. 351. 400. 401. 402. 403. and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the FEDERAL REGISTER of September 5, 1973 (38 FR 23971). The amendments: * * * (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Boards regulations are being made effective November 7, 1973.

PREAMBLE C

Amendment published 11-30-76

Preamble to the addition of Appendix—Interpretation No. 1 added on Nov. 30, 1976, at 41 FR 52427.

Interpretation No. 1 to Part 401, Cost Accounting Standard, Consistency in Estimating, Accumulating and Reporting Costs, is being published today by the Cost Accounting Standards Board pursuant to Section 719 of the Defense Production Act of 1950, as amended. (Pub. L. 91-379, 50 U.S.C. App. 2168.)

This Interpretation culminates extensive research over a period of several years on the subject of accounting for the costs of direct materials not incorporated in end items. This research indicated that, as a general rule, the cost of such materials is being allocated properly to cost objectives. Accordingly, the Board concluded that a Cost Accounting Standard on this subject was not warranted at this time. However, the research indicated that frequent questions were raised with respect to the requirements of Part 401 regarding consistency between estimating the costs of certain direct materials in pricing proposals and the accumulation and reporting of such costs. Thus, the Board concluded that it would be desirable to issue an Interpretation of Part 401 to address specifically the requirements regarding consistency between estimating and accounting for the costs of such direct materials.

Section 401.40 requires that a contractor's "practices used in estimating costs in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs." Many contractors estimate the cost of certain direct materials, such as materials that will be scrapped, as a percentage of basic direct material requirements or of some other base. A significant number of questions have been raised as to the cost accounting practices to be followed where the cost of such materials is estimated on the basis of percentage factors. The Interpretation being published clarifies the requirements of Part 401 in this regard.

A proposed Interpretation was published in the FEDERAL REGISTER of June 24, 1976, with an invitation to interested parties to submit written comments. The Board supplemented the invitation in the FEDERAL REGISTER by sending copies of the proposed Interpretation directly to over 1,000 organizations and individuals. The Board received 43 written comments, all of which have been carefully considered by the Board.

In addition to an evaluation of the written comments, conversations were held with thirteen of these commentators who indicated particular problems with the proposed Interpretation. The Board takes this opportunity to express its appreciation for the time and effort expended by those who met with the Board representaives or provided written comments.

Comments of particular significance with respect to the proposed Interpretation are discussed below.

1. NEED FOR AN INTERPRETATION

Several commentators stated that the Interpretation expands the scope and is not consistent with the intent of Part 401, which they say requires only a comparison of actual costs with estimated costs for direct material. They argued that the Defense Contract Audit Agency (DCAA) guidance to its field auditors in October 1973 satisfactorily explained the meaning of Part 401. In general, these commentators felt that an Interpretation to CAS 401 was not needed.

The Board's research indicates that an Interpretation is needed. Numerous and widespread questions have been raised concerning whether application of a percentage factor to a base as a means of estimating the costs of certain additional direct material requirements is in compliance with Part 401 when the contractor accumulates direct material costs in an undifferentiated account. The Board notes that a similar question with respect to direct labor is specifically addressed in Part 401, Section 401.60(b)(5). In that Illustration, the accumulation of total engineering labor in one undifferentiated account is not in compliance with Part 401 where the contractor estimates engineering labor by cost function. Part 401 does not, however, specifically address the consistency requirement for direct materials, nor did the DCAA guidance specifically cover this matter. Accordingly, the Board concludes that this Interpretation is needed.

In view of the fact that the Interpretation clarifies what is already required by Part 401, the Board does not agree that it expands the scope of the Standard.

2. MATERIALITY

A number of commentators maintained that the cost of the materials estimated by means of a percentage factor was usually insignificant. These commentators were concerned that extensive records or analyses would have to be developed for insignificant amounts. The Board, of course, has always been concerned about the question of materiality and is on record as stating that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. To assure the application of the materiality criterion in this instance, specific language has been introduced which provides that the Interpretation applies only where "a significant part of costs" is estimated by means of a percentage factor. Furthermore, the Interpretation being published today recognizes that the accounting requirements of Part 401 depend on the significance of each situation."

3. ESTIMATING TECHNIQUE VERSUS PRACTICE

Several respondents were of the opinion that the proposed Interpretation was inappropriate because they felt that the use of percentage factors to estimate the cost of certain direct materials is an estimating "technique," rather than an estimating "practice." Thus, they contended, the Interpretation is improperly covering an area not subject to Part 401, i.e., "estimating techniques," and would limit the use of estimating factors as quantitative estimating tools. Some of these respondents noted that the Board recognized the difference between techniques and practices in the prefatory comments to Part 401, as published in the FEDERAL REGISTER of February 29, 1972. In that publication, the Board noted the concern of some commentators that the term "practices" in the phrase "practices used in estimating costs in pricing proposals" could be confused as including estimating techniques relating to quantitative determinations. In response to those comments, the Board stated that "nothing in the Standard precludes the use of any quantitative estimating tools."

The Board reaffirms this conclusion. However, the Board did not intend to deny all interest in practices so readily subject to abuse. There are cases in which contractor percentage estimates are not adequately supported either by data as to relevant past experience or in any other manner. In such cases, particularly, the Board feels that the use of a percentage factor as a means of estimating the costs of additional direct materials is an estimating practice which must be consistent with the practices used in accumulating and reporting costs.

4. RETROACTIVITY

A few commentators were concerned about the possible retroactive application of this Interpretation. They noted that the requirement of Part 401, as interpreted, would apply as of the date a contractor was first required to use that Standard. The commentators were concerned that those contractors who have not accounted for material costs in accordance with the Interpretation could be held to have been in noncompliance with Part 401, and therefore subject to a downward price adjustment in accordance with paragraph a(5) of the Cost Account Standards clause (4 CFR 331.50). These commentators urged that the Interpretation be effective on a prospective basis only. Some of these commentators suggested that the substance of the Interpretation should be a new Standard, with the opportunity for an equitable adjustment under a(4)(A) of the Cost Accounting Standards clause.

As already noted, the Board has carefully considered whether the subject of the Interpretation should be encompassed in a new Standard. The Board has concluded that the accounting for direct material cost as explained by this Interpretation is required by Part 401 and therefore should have been accomplished as of the date that Standard first became applicable to a contractor. Nevertheless, the Board recognizes that there has been widespread uncertainty about the application of Part 401 in situations where certain material costs are estimated on the basis of percentage factors. In addition, the Board believes that the determination of the cost impact of a contractor's failure in the past to follow Part 401 as interpreted would be extremely difficult. Under the circumstances, the Board believes that the effort to seek contract price adjustments as a result of this Interpretation would, in most cases, be counterproductive. Accordingly, the Board believes that, in most cases, the process of attempting to determine price adjustments as a result of the retroactive application of Part 401 as interpreted would not be warranted.

5. COST ACCOUNTING PRACTICES

The proposed Interpretation stated that contractors who use a percentage factor to estimate certain direct material costs for a contract must "for that contract" maintain an adequate record or prepare an analysis of the actual cost. A number of commentators understood this sentence to require the recording or analysis on a contract-by-contract basis of the actual cost of materials represented by an estimated percentage factor. Many of these commentators noted that it would be difficult, if not impossible, to comply with this requirement. Other commentators questioned what was meant by an adequate record or an analysis.

As noted above the use of percentage factors for estimating direct material costs is an estimating practice which, pursuant to Part 401, must be consistent with the cost accounting practices used in accumulating and reporting costs. The Board notes however that Part 401 neither prescribes nor precludes any particular cost accounting practice. The Board recognizes that the consistency requirement of Part 401, as it pertains to direct material costs, could be met in a variety of ways. The Board is therefore of the view that it would be neither appropriate nor practical to prescribe by means of this Interpretation the amount of detail in accumulating and reporting costs which is deemed to be consistent with the use of percentage factors in estimating costs. The Board believes that the amount of detail which should be maintained with respect to direct material costs is a matter which is best left for decision by the appropriate Government procurement authorities on the basis of facts and circumstances of each situation. The Interpretation being published today has been revised accordingly and all references to the type of records to be maintained or analyses to be performed have been deleted.

6. APPLICATION TO DEVELOPMENTAL AND RESEARCH TYPE CONTRACTS

Many commentators urged that this Interpretation not apply to developmental and research type contracts. They said that since only material issued to these kinds of contracts is charged to such contracts, there would be no overstatement of material costs. They urged further that it would be impossible to maintain actual cost records by contract to record the additional material required and that it was extremely difficult to estimate additional material requirements because of the lack of past experience. Also, the commentators contended that material requirements on such contracts were not significant. Other commentators suggested that this Interpretation should not apply to cost type contracts.

It appears that these comments were generated mainly by the impression that the proposed Interpretation required records or analyses to be maintained by individual contract. As noted above, the Interpretation has been revised to make clear that no particular record or analysis is required by Part 401. The requirement for consistency in estimating, accumulating and reporting costs, however, applies to all contracts. The fact that a development contract or cost-type contract is involved does not remove this requirement. The Board feels that the changes made in the Interpretation should serve to minimize the problems described by these contractors.

7. APPLICATION TO STANDARD COST ACCOUNTING SYSTEMS

Several commentators suggested that this Interpretation not apply to standard cost systems. They argued that costs are not accumulated by contract or product and, therefore, compliance with the Interpretation would require a complicated and expensive recording system. They felt further that in setting standards, they use past experience plus engineering adjustments and could be charged by the Government with the need to comply with the records requirement of the Interpretation for each of their Standards.

Contractors using standard costs for material must comply with Part 407, the Use of Standard Costs for Direct Material and Direct Labor, which addresses the accounting for direct material and variances from standard costs of material. In the opinion of the Board, these contractors will be in compliance with Part 401 as interpreted.

8. APPLICATION TO SPECIFIC FACTORS

Various commentators inquired about the application of this Interpretation to certain specific factors used in estimating contract price proposals, not necessarily related to the cost of additional direct materials. Among the factors mentioned were those to provide for inflation, contingencies resulting from indefinite or incomplete bills of material, losses in common inventory accounts, and miscellaneous small parts and hardware items.

As noted in the Interpretation, its need was prompted by questions about the use of percentage factors to estimate the costs of "additional direct materials"; i.e., generally those direct materials not incorporated in end items. Factors such as those used to provide for inflation or allowances for incomplete bills of material do not represent costs of "additional direct materials," as that phrase is used in the Interpretation. In the opinion of the Board, this interpretation does not apply to the costs represented by such factors.

Factors used in a proposal to provide for inventory losses represent the costs of additional materials which are governed by this Interpretation. With respect to factors for small parts, the Board notes that in accordance with Part 401, § 401.60, Illustrations, a practice of estimating an average cost for a minor standard hardware item is considered to be consistent with the practice of recording the actual costs of such items.

The amount of detail to be used in accumulating and recording such costs, however, is a matter to be decided in accordance with this Interpretation.

9. APPLICATION OF INTERPRETATION TO DIRECT LABOR

A number of commentators raised questions concerning the applicability of the Interpretation to direct labor. Several commentators said it should not apply to such labor but should be clearly limited to direct materials. One commentator felt that the Interpretation was equally applicable to direct labor and should so state.

As already noted in paragraph 1, above, Part 401 includes specific provisions on the consistency requirements regarding direct labor. Accordingly, the Board is of the opinion that no further specific coverage of direct labor is required in this Interpretation.

PREAMBLE D

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 401.10. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 401.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

* * * * *

In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general aplicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 402—COST ACCOUNTING STANDARD—CONSISTENCY IN ALLOCATING COSTS INCURRED FOR THE SAME PURPOSE

Sec.
402.10 General applicability.
402.20 Purpose.
402.30 Definitions.
402.40 Fundamental requirement.
402.50 Techniques for application.
402.60 Illustrations.
402.70 Exemptions.
402.80 Effective date.

APPENDIX—INTERPRETATION NO. 1

PREAMBLES A—D

AUTHORITY: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

SOURCE: 37 FR 4173, Feb. 29, 1972, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in non-technical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (37 FR 4137, February 29, 1972) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 402.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

Preambles: For preamble to § 402.10, see preamble D of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 402.20 Purpose.

The purpose of this standard is to require that each type of cost is allocated only once and on only one basis to any contract or other cost objective. The criteria for determining the allocation of costs to a product, contract, or other cost objective should be the same for all similar objectives. Adherence to these cost accounting concepts is necessary to guard against the overcharging of some cost objectives and to prevent double counting. Double counting occurs most commonly when cost items are allocated directly to a cost objective without eliminating like cost items from indirect cost pools which are allocated to that cost objective.

§ 402.30 Definitions.

(a) The following definitions of terms which are prominent in this standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Allocate.* To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Cost objective.* A function, organizational subdivision contract or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost to processes, products, jobs, capitalized projects, etc.

(3) *Direct cost.* Any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or labor. Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives.

(4) *Final cost objective.* A cost objective which has allocated to it both direct and indirect costs, and, in the contractor's accumulation system, is one of the final accumulation points.

(5) *Indirect cost.* Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(6) *Indirect cost pool.* A grouping of incurred costs identified with two or more cost objectives but not identified specifically with any final cost objective.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this standard: None.

[37 FR 4173, Feb. 29, 1972, as amended at 38 FR 30730, Nov. 7, 197?]

PREAMBLES: For preambles to amendments of § 402.30, see preambles A and B of the supplement to this part.

§ 402.40 Fundamental requirement.

All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives. No final cost objective shall have allocated to it as an indirect cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included as a direct cost of that or any other final cost objective. Further, no final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective.

§ 402.50 Techniques for application.

(a) The Fundamental Requirement is stated in terms of cost incurred and is equally applicable to estimates of costs to be incurred as used in contract proposals.

(b) The Disclosure Statement to be submitted by the contractor will require that he set forth his cost accounting practices with regard to the distinction between direct and indirect costs. In addition, for those types of cost which are sometimes accounted for as direct and sometimes accounted for as indirect, the contractor will set forth in his Disclosure Statement the specific criteria and circumstances for making such distinctions. In essence, the Disclosure Statement submitted by the contractor, by distinguishing between direct and indirect costs, and by describing the criteria and circumstances for allocating those items which are sometimes direct and sometimes indirect, will be determinative as to whether or not costs are incurred for the same purpose. Disclosure Statement as used herein refers to the statement required to be submitted by contractors as a condition of contracting as set forth in Part 351 of this chapter.

(c) In the event that a contractor has not submitted a Disclosure Statement the determination of whether specific costs are directly allocable to contracts shall be based upon the contractor's cost accounting practices used at the time of contract proposal.

(d) Whenever costs which serve the same purpose cannot equitably be indirectly allocated to one or more final cost objectives in accordance with the contractor's disclosed accounting practices, the contractor may either: (1) Use a method for reassigning all such costs which would provide an equitable distribution to all final cost objectives, or (2) directly assign all such costs to final cost objectives with which they are specifically identified. In the event the contractor decides to make a change for either purpose the Disclosure Statement shall be amended to reflect the revised accounting practices involved.

(e) Any direct cost of minor dollar amount may be treated as an indirect cost for reasons of practicality where the accounting treatment for such cost is consistently applied to all final cost objectives, provided that such treatment produces results which are substantially the same as the results which would have been obtained if such cost had been treated as a direct cost.

§ 402.60 Illustrations.

(a) Illustrations of costs which are incurred for the same purpose:

(1) Contractor normally allocates all travel as an indirect cost and previously disclosed this accounting practice to the Government. For purposes of a new proposal, contractor intends to allocate the travel costs of personnel whose time is accounted for as direct labor directly to the contract. Since travel costs of personnel whose time is accounted for as direct labor working on other contracts are costs which are incurred for the same purpose, these costs may no longer be included within indirect cost pools for purposes of allocation to any covered Government contract. Contractor's Disclosure Statement must be amended for the proposed changes in accounting practices.

(2) Contractor normally allocates planning costs indirectly and allocates this cost to all contracts on the basis of direct labor. A proposal for a new contract requires a disproportionate amount of planning costs. The contractor prefers to continue to allocate planning costs indirectly. In order to equitably allocate the total planning costs, the contractor may use a method for allocating all such costs which would provide an equitable distribution to all final cost objectives. For example, he may use the number of planning documents processed rather than his former allocation base of direct labor. Contractor's Disclosure Statement must be amended for the proposed changes in accounting practices.

(b) Illustrations of costs which are not incurred for the same purpose:

(1) Contractor normally allocates special tooling costs directly to contracts. The costs of general purpose tooling are normally included in the indirect cost pool which is allocated to contracts. Both of these accounting practices were previously disclosed to the Government. Since both types of costs involved were not incurred for the same purpose in accordance with the criteria set forth in the contractor's Disclosure Statement, the allocation of general purpose tooling costs from the indirect cost pool to the contract, in addition to the directly allocated special tooling costs is not considered a violation of the standard.

(2) Contractor proposes to perform a contract which will require three firemen on 24-hour duty at a fixed-post to provide protection against damage to highly inflammable materials used on the contract. Contractor presently has a fire fighting force of 10 employees for general protection of the plant. Contractor's costs for these latter firement are treated as indirect costs and allocated to all contracts; however, he wants to allocate the three fixed-post firemen directly to the particular contract requiring them and also allocate a portion of the cost of the general firefighting force to the same contract. He may do so but only on condition that his disclosed practices indicate that the costs of the separate classes of firemen serve different purposes and that it is his practice to allocate the general firefighting force indirectly and to allocate fixed-post firemen directly.

§ 402.70 Exemptions.

None for this standard.

§ 402.80 Effective date.

July 1, 1972.

[37 FR 9609, May 13, 1972]

PREAMBLE: Preamble A of the supplement to this part explains how effective dates are determined.

APPENDIX—INTERPRETATION No. 1

Part 402, Cost Accounting Standard, Consistency in Allocating Costs Incurred for the Same Purpose, provides, in § 402.40, that "* * * no final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective."

This interpretation deals with the way Part 402 applies to the treatment of costs incurred in preparing, submitting, and supporting proposals. In essence, it is addressed to whether or not, under the Standard, all such costs are incurred for the same purpose, in like circumstances.

Under Part 402, costs incurred in preparing, submitting, and supporting proposals pursuant to a specific requirement of an existing contract are considered to have been incurred in different circumstances from the circumstances under which costs are incurred in preparing proposals which do not result from such specific requirement. The circumstances are different because the costs of preparing proposals specifically required by the provisions of an existing contract relate only to that contract while other proposal costs relate to all work of the contractor.

This interpretation does not preclude the allocation, as indirect costs, of costs incurred in preparing all proposals. The cost accounting practices used by the contractor, however, must be followed consistently and the method used to reallocate such costs, of course, must provide an equitable distribution to all final cost objectives.

[41 FR 24692, June 18, 1976]

PREAMBLE: For the preamble relating to Interpretation No. 1, see preamble C of the supplement.

PREAMBLE A

Preamble to Original Publication of Part 402, 2-29-72

Preamble to original publication of 4 CFR Part 402, 37 FR 4139, Feb. 29, 1972. That publication also included the addition of 4 CFR Parts 331, 351, 400, and 401, and so material relating to those parts has been omitted. It appears in the Supplements to those parts.

General comments. The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C. app. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in

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such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives—improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable representatives of various Government agencies, Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, FEDERAL REGISTER for comment.

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Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board's disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

* * * * *

Part 402 Title. One commentator pointed out that the definition of the word "allocate" covered all of the actions encompassed by the word "charge" and, therefore, the title of the standard should be changed to delete the words "charging and." The Board agrees and has made the appropriate change here and elsewhere throughout the standard.

Section 402.40 Fundamental requirement. A number of commentators suggested a change to the standard to eliminate the requirement that direct and indirect costs be consistently allocated to all final cost objectives. Making the standard applicable only to individual contracts would permit a choice to be made solely on the basis of short-term economic benefit; the Board therefore has not adopted the suggestion.

Section 402.50 Techniques for application. Several commentators noted that the standard discusses the required treatment of incurred costs but does not cover estimated costs. The Board intends that both types of costs be covered by the standard and has therefore added a new paragraph to this section to make that intention clear.

A number of commentators suggested that the concept of materiality be included in the standard to allow the handling of minor direct cost items as indirect costs similar to the treatment accorded materiality in current ASPR regulations. The Board agrees, and has included a materiality statement in this section.

Several commentators did not understand the relationship of this standard to the Disclosure Statement. (This relationship is set out in paragraph (b) of this section) The Board intends to allow the contractor to disclose the cost accounting practices and criteria appropriate to his own situation while at the same time imposing the requirement that he adhere consistently to the choices once made. The Disclosure Statement is the vehicle by which the contractor describes the criteria and circumstances which define costs which are or are not incurred for the same purpose.

* * * * *

Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in § 331.8, § 351.4(e), and Parts 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules, or regulations.

* * * * *

4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

PREAMBLE B

Amendments Published 11-7-73

Preamble to revision of the definitions of "cost objective" and "indirect cost pool", § 402.30(a) (2) and (6); 38 FR 30725, Nov. 7, 1973. Material relating to other parts of 4 CFR Chapter III, published in the same document, has been omitted, and appears in the Supplements to those parts.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the FEDERAL REGISTER of September 5, 1973 (38 FR 23971). The amendments: * * * (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973.

PREAMBLE C

Amendment Published 6-18-76

Preamble to the addition of Appendix—Interpretation No. 1 added on June 18, 1976 at 41 FR 24691.

Interpretation No. 1 to Part 402, Cost Accounting Standard, Consistency in Allocating Costs Incurred for the Same Purpose, is being published today by the Cost Accounting Standards Board pursuant to Section 719 of the Defense Production Act of 1950, as amended. (Pub. L. 91-379, 50 U.S.C. App. 2168). The interpretation deals with the application of § 402.40 of Part 402 to proposal costs. Section 402.40 provides that, "All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives."

A number of questions had been raised by both the Government and contractors as to how Cost Accounting Standard 402 is to be applied to the accounting for proposal costs and, particularly, as to whether all costs incurred in preparing proposals are incurred for the same purpose, in like circumstances. A proposed interpretation was published in the FEDERAL REGISTER of February 4, 1976, with an invitation to interested parties to submit written comments if the proposed interpretation did not respond fully, or did not respond clearly enough, to what the Board understood to be the questions which had arisen. The Board also supplemented the invitation in the FEDERAL REGISTER by sending copies of the proposed interpretation to several hundred organizations and individuals. The Board received 32 written comments from companies, Government agencies, industry and professional associations, and others. All of these comments have been carefully considered by the Board. The issues of particular significance which were discussed by respondents in connection with the proposed interpretation are summarized below, together with explanations of the changes made in the interpretation being published today. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms that were received.

(1) *Specific requirement provision.* Several commentators, while suggesting changes to the proposed interpretation published on February 4, 1976, commended the Board for recognizing the problem with respect to the application of § 402.40 of Part 402 to the costs incurred in preparing proposals and believed that the interpretation would resolve a longstanding area of controversy. The most prevalent comments received dealt with costs incurred in preparing a follow-on proposal which is not specifically required by an existing contract.

Many commentators suggested that the words "specific requirement" be deleted and that, in lieu thereof, words such as "related to," "arising from," "identified with," or "directly associated with," be used. Other commentators, while agreeing that the "specific requirement" provision should be retained, suggested an expansion to also cover proposals "related to" existing contracts such as proposals for follow-on contracts. Still other commentators, however, believed that the "specific requirement" provision was appropriate and should be retained without addition or other change.

In the February 4, 1976, publication of the proposed interpretation, the distinguishing characteristic noted by the Board for determining if circumstances can be considered to be different with respect to costs incurred in preparing two proposals was whether one proposal was prepared pursuant to a specific requirement of an existing contract while the other was not. The Board continues in the belief that the "specific requirement" provision is the distinguishing characteristic and, accordingly, has retained this provision in the interpretation being published today.

Several commentators suggested that proposals prepared in order to comply with other contract provisions, such as when the Government exercises an unpriced option or when an option is repriced, should be considered to be specifically required under the interpretation. The Board believes that the interpretation being published today accommodates this suggestion.

One commentator suggested that the Board's intent be clarified with respect to whether only proposals required by line items in a contract are considered to be specifically required by the contract. The Board intended that, while the "specific requirement" could be a line item in a contract, it need not be. Proposals specifically required by any other provisions of a contract, such as the requirement in the Changes clause of Standard Form 32, that any "claim by the contractor for adjustment under this clause must be asserted within 30 days from the date of receipt by the contractor of the notification of change," are considered to be specifically required under the interpretation.

(2) *Indirect allocation of all proposal costs.* A few commentators recommended clarification of the final paragraph in the proposed interpretation as published on February 4, 1976. One commentator stated that the paragraph could be interpreted as authorizing contractors to allocate all proposal costs indirectly while another commentator believed that the subject of indirect allocation of all proposal costs should be developed later as a separate issue. The paragraph has been revised (a) to give recognition to the fact that some contractors' accounting practices now provide that all proposal costs are pooled and allocated indirectly and (b) to make it clear that, in this respect, no change in a contractor's accounting practice or allocation method is required by this interpretation if the cost accounting practice is being followed consistently and if the allocation method provides an equitable distribution to all final cost objectives.

(3) *Determination of cost accounting practices by contracting officer.* A few commentators stated that the words, "specific requirement of an existing contract" would place contracting officers in the position of determining cost accounting practices because they could determine whether there would be a specific requirement in a contract.

Contracting officers now decide for almost every contract whether to include or exclude specific contractual requirements covering a wide variety of activities. The Board believes that inclusion or exclusion of a specific requirement in a contract may influence the cost accounting practice being followed but the decision to include or exclude the requirement is not the determinant of the cost accounting practice.

(4) *Prospective application.* Two commentators suggested that, under this interpretation, certain proposal costs which some contractors have allocated directly to contracts will have to be allocated indirectly. One of the commentators recommended that, consequently, the interpretation should be applied on a prospective basis only.

Cost Accounting Standard 402, which became effective July 1, 1972, states that, "All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives." Interpretation No. 1 to Part 402 recognizes that the circumstances involved in preparing certain proposals are different from the circumstances involved in preparing other proposals. The interpretation explains when, under the Standard, certain proposal costs are consequently deemed to have been incurred in unlike circumstances and therefore may be accounted for differently.

Although the interpretation is being provided to explain in greater detail how Cost Accounting Standard 402 applies to costs incurred in preparing proposals, the Standard from its inception has applied to these costs in this way. As to any individual contractor, Standard 402 has applied to such costs from whatever date that Standard became applicable to that contractor. The commentator's recommendation therefore has not been accepted. In view of the widespread uncertainty over the application of Standard 402 to proposal costs, however, the Board believes that any failures to follow the Standard in this respect have been inadvertent. The Board also believes that any adjustments should be made with due consideration to the Board's statement on materiality.

(5) *Accounting for the cost of proposals for follow-on contracts.* Several commentators stated that the inter-

pretation would create cost accounting problems with respect to accounting for the cost of proposals for follow-on contracts. The statement was made that a follow-on proposal is prepared by employees assigned full time to the on-going program and that it would be most difficult and impractical to attempt to separate their labor costs for preparing follow-on proposals from their other labor costs of the on-going program.

The Board recognizes the possibility that some contractors may have to refine somewhat their present practices for distributing incurred labor costs in order to separate the costs of preparing proposals for a follow-on contract from the costs of an existing contract. The Board does not agree, however, that whatever refinements may be necessary should be difficult or impractical to develop.

(6) *Other comments.* One commentator suggested that it be clearly stated in the interpretation that proposal costs allocated direct to contracts will have overhead and General and Administrative expenses (including indirect proposal costs) applied. The Board agrees that proposal costs allocated direct to a contract are no different than any other costs allocated direct to that contract but believes this is self-evident and that no change in the interpretation is required.

Another commentator suggested that the word "bid" be added to the interpretation in conjunction with the word "proposal." The Board intends that the interpretation apply to a "proposal" as defined in 4 CFR, Part 400.

A few commentators requested clarification of the wording of the introductory comments and the proposed interpretation published on February 4, 1976. The introductory comments stated that, "Costs * * * are incurred in different circumstances * * *" whereas the proposed interpretation stated that, "The contracting parties can determine that the circumstances are different * * *." Accordingly, the Board has deleted the words, "The contracting parties can determine that * * *" from the interpretation being published today.

Another commentator suggested that the phrase, "to all work of the contractor," in the last sentence of the third paragraph of the interpretation be clarified because some companies have several indirect cost pools for proposal costs, one for each major product line within a division. The commentator believed that the phrase could be misinterpreted as limiting the number of such indirect cost pools to only one pool for each division. It is not the intent of the Board to change, through this interpretation, any of the established cost accounting practices now being followed by contractors with respect to the pooling and allocation of indirect proposal costs. Accordingly, if it is the contractor's established cost accounting practice to pool and allocate indirect proposal costs by product groupings, he may continue to do so.

One commentator requested a statement in the interpretation with respect to solicited and unsolicited proposals, particularly as to "whether one or the other is properly included in the direct or indirect charge category." The determination as to like or unlike circumstances does not depend on whether a proposal is solicited or unsolicited. The test is whether the proposal was specifically required by an existing contract.

PREAMBLE D

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 402.10. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 402.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

* * * * *

In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 403—ALLOCATION OF HOME OFFICE EXPENSES TO SEGMENTS

Sec.

403.10 General applicability.
403.20 Purpose.
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403.80 Effective date.
APPENDIX—INTERPRETATION NO. 1
PREAMBLES A—E

AUTHORITY: Sec. 103, 84 Stat. 796; 50 U.S.C. App. 2168.

SOURCE: 37 FR 22683, Dec. 14, 1972, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in non-technical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (37 FR 22683, December 14, 1972) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 403.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

PREAMBLES: For preamble to § 403.10, see preamble E of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 403.20 Purpose.

(a) The purpose of this Cost Accounting Standard is to establish criteria for allocation of the expenses of a home office to the segments of the organization based on the beneficial or causal relationship between such expenses and the receiving segments. It provides for: (1) Identification of expenses for direct allocation to segments to the maximum extent practical; (2) accumulation of significant nondirectly allocated expenses into logical and relatively homogeneous pools to be allocated on bases reflecting the relationship of the expenses to the segments concerned; and (3) allocation of any remaining or residual home office expenses to all segments. Appropriate implementation of this Standard will limit the amount of home office expenses classified as residual to the expenses of managing the organization as a whole.

(b) This Standard does not cover the reallocation of a segment's share of home office expenses to contracts and other cost objectives.

§ 403.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Allocate.* To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Home office.* An office responsible for directing or managing two or more, but not necessarily all, segments of an organization. It typically establishes policy for, and provides guidance to the segments in their operations. It usually performs management, supervisory, or administrative functions, and may also perform service functions in support of the operations of the various segments. An organization which has intermediate levels, such as groups, may have several home offices which report to a common home office. An intermediate

organization may be both a segment and a home office.

(3) *Operating revenue.* Amounts accrued or charged to customers, clients, and tenants, for the sale of products manufactured or purchased for resale, for services, and for rentals of property held primarily for leasing to others. It includes both reimbursable costs and fees under cost-type contracts and percentage-of-completion sales accruals except that it includes only the fee for management contracts under which the contractor acts essentially as an agent of the Government in the erection or operation of Government-owned facilities. It excludes incidental interest, dividends, royalty, and rental income, and proceeds from the sale of assets used in the business.

(4) *Segment.* One of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(5) *Tangible capital asset.* An asset that has physical substance, more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the services it yields.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this standard: None.

[37 FR 22683, Dec. 14, 1972, as amended at 38 FR 30730, Nov. 7, 1973]

PREAMBLES: For preambles to amendments to § 403.30, see preambles A and B of the supplement to this part.

§ 403.40 Fundamental requirement.

(a) (1) Home office expenses shall be allocated on the basis of the beneficial or causal relationship between supporting and receiving activities. Such expenses shall be allocated directly to segments to the maximum extent practical. Expenses not directly allocated, if significant in amount and in relation to total home office expenses, shall be grouped in logical and homogeneous expense pools and allocated pursuant to paragraph (b) of this section. Such allocations shall minimize to the extent practical the amount of expenses which may be categorized as residual (those of managing the organization as a whole). These residual expenses shall be allocated pursuant to paragraph (c) of this section.

(2) No segment shall have allocated to it as an indirect cost, either through a homogeneous expense pool, or the residual expense pool, any cost, if other costs incurred for the same purpose have been allocated directly to that or any other segment.

(b) The following subparagraphs provide criteria for allocation of groups of home office expenses.

(1) *Centralized service functions.* Expenses of centralized service functions performed by a home office for its segments shall be allocated to segments on the basis of the service furnished to or received by each segment. Centralized service functions performed by a home office for its segments are considered to consist of specific functions which, but for the existence of a home office, would be performed or acquired by some or all of the segments individually. Examples include centrally performed personnel administration and centralized data processing.

(2) *Staff management of certain specific activities of segments.* The expenses incurred by a home office for staff management or policy guidance functions which are significant in amount and in relation to total home office expenses shall be allocated to segments receiving more than a minimal benefit over a base, or bases, representative of the total specific activity being managed. Staff management or policy guidance to segments is commonly provided in the overall direction or support of the performance of discrete segment activities such as manufacturing, accounting, and engineering (but see paragraph (b)(6) of this section).

(3) *Line management of particular segments or groups of segments.* The expense of line management shall be allocated only to the particular segment or group of segments which are being managed or supervised. If more than one segment is managed or supervised, the expense shall be allocated using a base or bases representative of the total activity of such segments. Line management is considered to consist of management or supervision of a segment or group of segments as a whole.

(4) *Central payments or accruals.* Central payments or accruals which are made by a home office on behalf of its segments shall be allocated directly to segments to the extent that all such payments or accruals of a given type or class can be identified specifically with individual segments. Central payments or accruals are those which but for the existence of a number of segments would be accrued or paid by the individual segments. Common examples include centrally paid or accrued pension costs, group insurance costs, State and local income taxes and franchise taxes, and payrolls paid by a home office on behalf of its segments. Any such types of payments or accruals which cannot be identified specifically with individual segments shall be allocated to benefited segments using an allocation base representative of the factors on which the total payment is based.

(5) *Independent research and development costs and bid and proposal costs.* Independent research and development costs and bid and proposal costs of a home office shall be allocated in accordance with 4 CFR Part 420.

(6) *Staff management not identifiable with any certain specific activities of segments.* The expenses incurred by a home office for staff management, supervisory, or policy functions, which are not identifiable to specific activities of segments shall be allocated in accordance with paragraph (c) of this section as residual expenses.

(c) *Residual expenses.* (1) All home office expenses which are not allocable in accordance with paragraph (a) of this section and paragraphs (1) through (5) of paragraph (b) of this section shall be deemed residual expenses. Typical residual expenses are those for the chief executive, the chief financial officer, and any staff which are not identifiable with specific activities of segments. Residual expenses shall be allocated to all segments under a home office by means of a base representative of the total activity of such segments, except where paragraph (c)(2) or (3) of this section applies.

(2) Residual expenses shall be allocated pursuant to paragraph (1) of § 403.50(c) if the total amount of such expenses for the contractor's previous fiscal year (excluding any unallowable costs and before eliminating any amounts to be allocated in accordance with paragraph (c)(3) of this section) exceeds the amount obtained by applying the following percentage(s) to the aggregate operating revenue of all segments for such previous year:

3.35 percent of the first $100 million.
0.95 percent of the next $200 million.
0.30 percent of the next $2.7 billion.
0.20 percent of all amounts over $3 billion.

The determination required by this paragraph for the 1st year the contractor is subject to this Standard shall be based on the pro forma application of this Standard to the home office expenses and aggregate operating revenue for the contractor's previous fiscal year.

(3) Where a particular segment receives significantly more or less benefit from residual expenses than would be reflected by the allocation of such expenses pursuant to paragraph (c)(1) or (2) of this section (see § 403.50(d)), the Government and the contractor may agree to a special allocation of residual expenses to such segment commensurate with the benefits received. The amount of a special allocation to any segment made pursuant to such an agreement shall be excluded from the pool of residual expenses to be allocated pursuant to paragraph (c)(1) or (2) of this section, and such segment's data shall be excluded from the base used to allocate this pool.

[37 FR 22683, Dec. 14, 1972, as amended at 44 FR 55127, Sept. 25, 1979]

PREAMBLE: For preamble relating to § 403.40(b)(5), see Preamble A of the supplement to Part 420.

§ 403.50 Techniques for application.

(a) (1) Separate expense groupings will ordinarily be required to implement § 403.40. The number of groupings will depend primarily on the variety and significance of service and management functions performed by a particular home office. Ordinarily, each service or management function will have to be separately identified for allocation by means of an appropriate allocation technique. However, it is not necessary to identify and allocate different functions separately, if allocation in accordance with the relevant requirements of § 403.40(b) can be made using a common allocation base. For example, if the personnel department of a home office provides personnel services for some or all of the segments (a centralized service function) and also established personnel policies for the same segments (a staff management function), the expenses of both functions could be allocated over the same base, such as the number of personnel, and the separate functions do not have to be identified.

(2) Where the expense of a given function is to be allocated by means of a particular allocation base, all segments shall be included in the base unless: (i) Any excluded segment did not receive significant benefits from, or contribute significantly to the cause of the expense to be allocated and, (ii) any included segment did receive significant benefits from or contribute significantly to the cause of the expense in question.

(b) (1) Section 403.60 illustrates various expense pools which may be used together with appropriate allocation bases. The allocation of centralized service functions shall be governed by a hierarchy of preferable allocation techniques which represent beneficial or casual relationships. The preferred representation of such relationships is a measure of the activity of the organization performing the function. Supporting functions are usually labor-oriented, machine-oriented, or space-oriented. Measures of the activities of such functions ordinarily can be expressed in terms of labor hours, machine hours, or square footage. Accordingly, costs of these functions shall be allocated by use of a rate, such as a rate per labor hour, rate per machine hour or cost per square foot, unless such measures are unavailable or impractical to ascertain. In these latter cases the basis for allocation shall be a measurement of the output of the supporting function. Output is measured in terms of units of end product produced by the supporting function, as for example, number of printed pages for a print shop, number of purchase orders processed by a purchasing department, number of hires by an employment office.

(2) Where neither activity nor output of the supporting function can be practically measured, a surrogate for the beneficial, or causal relationship must be selected. Surrogates used to represent the relationship are generally measures of the activity of the segments receiving the service; for example, for personnel services reasonable surrogates would be number of personnel, labor hours, or labor dollars of the segments receiving the service. Any surrogate used should be a reasonable measure of the services received and, logically, should vary in proportion to the services received.

(c) (1) Where residual expenses are required to be allocated pursuant to § 403.40(c)(2), the three factor formula described below must be used. This formula is considered to result in appropriate allocations of the residual expenses of home offices. It takes into account three broad areas of management concern: The employees of the organization, the business volume, and the capital invested in the organization. The percentage of the residual expenses to be allocated to any segment pursuant to the three factor formula is the arithmetical average of the following three percentages for the same period:

(i) The percentage of the segment's payroll dollars to the total payroll dollars of all segments.

(ii) The percentage of the segment's operating revenue to the total operating revenue of all segments. For this purpose, the operating revenue of any segment shall include amounts charged to other segments and shall be reduced by amounts charged by other segments for purchases.

(iii) The percentage of the average net book value of the sum of the segment's tangible capital assets plus inventories to the total average net book value of such assets of all segments. Property held primarily for leasing to others shall be excluded from the computation. The average net book value shall be the average of the net book value at the beginning of the organization's fiscal year and the net book value at the end of the year.

(d) The following paragraphs provide guidance for implementing the requirements of § 403.40(c)(3).

(1) An indication that a segment received significantly less benefit in relation to other segments can arise if a segment, unlike all or most other segments, performs on its own many of the functions included in the residual expense. Another indication may be that, in relation to its size, comparatively little or no costs are allocable to a segment pursuant to § 403.40(b) (1) through (5). Evidence of comparatively little communication or interpersonal relations between a home office and a segment, in relation to its size, may also indicate that the segment receives significantly less benefit from residual expenses. Conversely, if the opposite conditions prevail at any segment, a greater allocation than would result from the application of § 403.40(c) (1) or (2) may be indicated. This may be the case, for example, if a segment relies heavily on the home office for certain residual functions normally performed by other segments on their own.

(2) Segments which may require special allocations of residual expenses pursuant to § 403.40(c)(3) include, but are not limited to foreign subsidiaries, GOCO's, domestic subsidiaries with less than a majority ownership, and joint ventures.

(3) The portion of residual expenses to be allocated to a segment pursuant to § 403.40(c)(3) shall be the cost of estimated or recorded efforts devoted to the segments.

(e) Home office functions may be performed by an organization which for some purposes may not be a part of the legal entity with which the Government has contracted. This situation may arise, for example, in instances where the Government contracts directly with a corporation which is wholly or partly owned by another corporation. In this case, the latter corporation serves as a "home office," and the corporation with which the contract is made is a "segment" as those terms are defined and used in this Standard. For purposes of contracts subject to this Standard, the contracting corporation may only accept allocations from the other corporation to the extent that such allocations meet the requirements set forth in this Standard for allocation of home office expenses to segments.

[37 FR 4173, Feb. 29, 1972, as amended at 43 FR 9781, Mar. 10, 1978]

PREAMBLES: For preambles relating to § 403.50, see preambles A and B of the supplement to this part. For the preamble on the deletion of § 403.50(c)(2), see preamble J of the supplement to Part 331.

§ 403.60 Illustrations.

(a) The following table lists some typical pools, together with illustrative allocation bases which could be used in appropriate circumstances:

Home office expense or function	Illustrative allocation bases
Centralized service functions:	
1. Personnel administration	1. Number of personnel, labor hours, payroll, number of hires.
2. Data processing services	2. Machine time, number of reports.
3. Centralized purchasing and subcontracting	3. Number of purchase orders, value of purchases, number of items.
4. Centralized warehousing	4. Square footage, value of material, volume.
5. Company aircraft service	5. Actual or standard rate per hour, mile, passenger mile, or similar unit.
6. Central telephone service	6. Usage costs, number of instruments.

(b) The selection of a base for allocating centralized service functions shall be governed by the criteria established in § 403.50(b).

(c) The listed allocation bases in this section are illustrative. Other bases for allocation of home office expenses to segments may be used if they are substantially in accordance with the beneficial or casual relationships outlined in § 403.40.

Home office expense or function	Illustrative allocation bases
Staff management of specific activities:	
1. Personnel management	1. Number of personnel, labor hours, payroll, number of hires.
2. Manufacturing policies (quality control, industrial engineering, production, scheduling, tooling, inspection and testing, etc.)	2. Manufacturing cost input, manufacturing direct labor.
3. Engineering policies	3. Total engineering costs, engineering direct labor, number of drawings.
4. Material/purchasing policies	4. Number of purchase orders, value of purchases.
5. Marketing policies	5. Sales, segment marketing costs.
Central payments or accruals:	
1. Pension expenses	1. Payroll or other factor on which total payment is based.
2. Group insurance expenses	2. Payroll or other factor on which total payment is based.
3. State and local income taxes and franchise taxes	3. Any base or method which results in an allocation that equals or approximates a segment's proportionate share of the tax imposed by the jurisdiction in which the segment does business, as measured by the same factors used to determine taxable income for that jurisdiction.

§ 403.70 Exemptions.

(a) Any contractor or subcontractor which together with its subsidiaries did not receive net awards of negotiated national defense prime contracts during Federal fiscal year 1971 (July 1, 1970, through June 30, 1971) totaling more than $30 million is exempt from this Standard. This exemption expires on March 10, 1978. Any contractor, unless otherwise exempt, who receives a negotiated national defense contract after March 10, 1978, snall be required to comply at the start of his first cost accounting period following receipt of that award.

(b) This standard shall not apply to contractors who are subject to the provisions of Federal Management Circular 74-4 (Principles for Determining Costs Applicable to Grants and Contracts with State and Local Governments).

[37 FR 4173, Feb. 29, 1972, as amended at 40 FR 32749, Aug. 4, 1975; 42 FR 45629, Sept. 12, 1977; 43 FR 24820, June 8, 1978]

PREAMBLES: For preamble affecting § 403.70, see preambles A, C, D, and E of the supplement to this part. For preamble to superseded regulations, see preamble B of the supplement to this part.

§ 403.80 Effective date.

(a) This standard shall be followed by each contractor as of the beginning of his next fiscal year after September 30, 1973. The effective date of this standard is July 1, 1973.

(b) The effective date of § 403.70(a) as amended is March 10, 1978.

[38 FR 7447, Mar. 22, 1973; as amended at 42 FR 45629, Sept. 12, 1977]

PREAMBLES: Preamble A of this part explains how effective dates are determined. For preamble affecting § 403.80(b), see preamble D.

APPENDIX—INTERPRETATION NO. 1

Questions have arisen as to the requirements of Part 403, Cost Accounting Standard, Allocation of Home Office Expenses to Segments, for the purpose of allocating State and local income taxes and franchise taxes based on income (hereinafter collectively referred to as income taxes) from a home office of an organization to its segments.

By means of an illustrative allocation base in Section 403.60, the Standard provides that income taxes are to be allocated by "any base or method which results in an allocation that equals or approximates a segment's proportionate share of the tax imposed by the jurisdiction in which the segment does business, as measured by the same factors used to determine taxable income for that jurisdiction." This provision contains two essential criteria for the allocation of income taxes from a home office to segments. First, the taxes of any particular jurisdiction are to be allocated only to those segments that do business in the taxing jurisdiction. Second, where there is more than one segment in a taxing jurisdiction, the taxes are to be allocated among those segments on the basis of "the same factors used to determine the taxable income for that jurisdiction." The questions that have arisen relate primarily to whether segment book income or loss is a "factor" for this purpose.

Most States tax a fraction of total organization income, rather than the book income of segments that do business within the State. The fraction is calculated pursuant to a formula prescribed by State statute. In these situations the book income or loss of individual segments is not a factor used to determine taxable income for that jurisdiction. Accordingly, in States that tax a fraction of total organization income, rather than the book income of segments within the State, such book income is irrelevant for tax allocation purposes. Therefore, segment book income is to be used as a factor in allocating income tax expense from a home office to segments only where this amount is expressly used by the taxing jurisdiction in computing the income tax.

[45 FR 13721, Mar. 3, 1980]

PREAMBLE A

Preamble to Original Publication, 12-14-72

Preamble to original publication of 4 CFR Part 403, at 38 FR 26680, Dec. 14, 1972.

The Standard on Allocation of Home Office Expenses to Segments is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub. L. 91-379, 50 U.S.C. app. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work on this Standard was initiated as the result of a variety of continuing problems between contractors and the Government concerning equitable allocations of home office expenses to segments involved in negotiated defense contracts. The problems include disagreements on:

(i) The propriety in certain circumstances of using particular allocation bases, such as cost of sales or direct labor for allocating home office expenses to segments; (ii) whether and to what extent certain kinds of segments such as GOCO's, foreign subsidiaries and partially owned subsidiaries should be included in the allocation base; and (iii) the homogeneity of expense pools.

The allocation of home office expenses to segments is not now specifically governed or guided by an authoritative accounting statement. Home office expenses allocated to segments and then to contracts can constitute an important element of total contract cost. The lack of authoritative standards to guide contractors, procurement officers, auditors, and others, provides a great potential for disagreement and controversy over contract costs. Assurance of equity in cost determinations and contract settlement is singularly lacking.

This Standard prescribes criteria for allocation of the expenses of a home office to segments of an organization. The criteria are based primarily on the beneficial or causal relationship between such expenses and the receiving segments. The Standard governs how a contractor may allocate expenses of its corporate headquarters to various divisions, subsidiaries, plants, or other subsidiaries of the corporation. The Board believes that application of this Standard will result in sound cost accounting and will provide a great degree of uniformity in the determination of costs of negotiated defense contracts.

Research establishes that some home office expenses are incurred for specific segments and can be assigned directly to them. Other expenses, not incurred for a specific segment, have clear relationships to two or more segments, relationships which are measurable with reasonable objectivity. A third type of home office expense possesses no readily measurable relationship to segments.

The Cost Accounting Standards Board finds that a Cost Accounting Standard to govern the allocation of home office expenses is desirable to reduce wasteful and expensive controversy and to obtain equity for the contracting parties. The Standard published today requires that those home office expenses incurred for specific segments are to be allocated directly to those segments to the maximum extent practical. Those that can be allocated to segments on the basis of objective measurable relationships are to be accumulated and allocated by means of logical and homogenous expense pools established for this purpose. The remaining or residual home office expenses are then to be allocated as discussed below.

The Board expects that this Standard will operate to reduce residual expenses to a relatively minor amount and by this means also reduce controversy and inequity. Where this is the case, the Board sees no reason to require one particular technique to allocate these expenses. Accordingly, where residual expenses are no greater than a specified percentage of operating revenues, the Standard allows the use of any appropriate allocation technique. However, if residual expenses exceed such specified percentages, the Board believes that its objective of reducing controversy and avoiding inequity would best be served by selecting a single allocation technique to be used. Its research in this connection has led the Board to conclude that for this purpose, a three-factor formula is superior to other allocation bases and techniques for the allocation of residual expenses.

Early research on this Standard included an extensive review of available literature on the subject, a review of decisions of contract appeals boards and courts, and a study of home office management philosophy and operations of 40 companies representing a wide variety of industries.

This research led to the publication of a proposed Cost Accounting Standard in the FEDERAL REGISTER of June 30, 1972, with an invitation for interested parties to submit written data, views, and comments to the Board. To better assure that those who had already expressed interest or provided assistance had an opportunity to comment, the Board supplemented the FEDERAL REGISTER notice by sending copies of the FEDERAL REGISTER materials directly to 196 organizations and individuals, of which 86 companies were invited to furnish the Board with estimates of any additional or reduced costs which could arise from the implementation of the Standard.

Responses were received from 130 sources, including individual companies, Government agencies, professional associations, industry associations, public accounting firms, and others. All of these comments and data have been carefully considered by the Board. Those comments which are of particular significance are discussed below together with an explanation of resultant substantive changes to the Standard as published in the FEDERAL REGISTER of June 30, 1972.

As will be seen from the following discussion, the Board was greatly benefited by the many comments it received on the Standard as published in the FEDERAL REGISTER of June 30, 1972. The Board takes this opportunity to express its considerable debt to those who devoted time and skill to assisting the Board in this endeavor and to thank the many companies and individuals involved.

(1) *Materiality.* Many commentators urged that the Standard contain a general statement on materiality. The Board has previously stated that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. The Board does not believe that any further general statement is needed at this time. However, where specific changes could be made to clarify the intent of this Standard with respect to materiality, they have been made as further discussed below.

While most commentators agreed with the concept of maximum direct allocation of home office expenses, and accumulation of nondirectly allocated home office expenses into logical, homogeneous expense pools, a few of these commentators believed that the Standard did not adequately incorporate the concept of materiality for this purpose. The Board agrees that materiality is an important consideration in determining whether to specify that an expense is to be allocated directly or by means of a separate expense pool. Accordingly, § 403.40 of the Standard has been revised to state that expenses are to be allocated to the maximum extent "practical" and that expenses not directly allocated are to be grouped into separate homogeneous expense pools "if significant in amount and in relation to total home office expenses."

In addition, a number of commentators questioned the need for using what they considered to be a relatively complex formula to allocate residual expenses even when they are minor in amount. This requirement was contained in the Standard as published in the FEDERAL REGISTER of June 30, 1972. The Board believes the formula to be relatively simple, well understood, already used by many companies to satisfy State tax requirements, and based on financial data that is readily available. Nevertheless, the Board agrees that other allocation techniques may be acceptable if residual expenses are not material. Accordingly, § 403.40(c) of the Standard being published today permits the use of any allocation base representative of total activity if residual expenses are less than a specified percentage of operating revenue.

The Board also considered a materiality test conducted periodically which would permit a contractor, otherwise covered, to choose not to follow the Standard if its application would result in little or no change in the total amount he allocates to his segments with Government business. The Board in this instance rejected this approach for the following reasons:

(a) Such an approach would put undue emphasis on the effect of this Standard on the allocation of costs to or away from Government contracts.

(b) The administrative problems and time spent by both the Government and the contractor in estimating the contract cost consequences of application of the Standard periodically and negotiating the pro forma application of the Standard for comparative test purposes would outweigh any benefits that might be derived from waiver of the entire Standard on the basis of materiality of result.

(c) There would be no assurance that a contractor's own procedures, which in the test year happened to provide nearly identical results to the results which would be provided through use of the Standard, would in other, subsequent years also produce the same nearly identical results. In effect, the results in the test year may have been an aberration.

(d) In light of the general acceptance by the majority of commentators of the concept of direct charging and grouping of homogeneous expense pools, the provisions for materiality considerations previously described are deemed sufficient.

(e) The Board has applied the concept of materiality to the extent it believes practical in this Standard. The Board, however, as noted in its prefactory comments on the first two published Standards (37 FR 4141), will give consideration to stating a concept of materiality applicable to all Standards if subsequent events indicate the desirability and feasibility of doing so.

The Board has eliminated a requirement, originally contained in the June 30, 1972, proposal, for interdepartmental allocations of home office expenses. This proposal would have required part of the cost of certain home office functions to be allocated to other home office functions before being reallocated to segments. The Board accepts the views of a number of commentators that this procedure would be complex and unwarranted in the light of a relatively insignificant effect on the allocation of home office expenses.

The proposed Standard, as published in the FEDERAL REGISTER of June 30, 1972, required that all segments be included in an allocation base unless it could be demonstrated that any segment did not receive benefit from, or contribute to the cause of, an expense to be allocated. A number of commentators observed that it would be virtually impossible to demonstrate that a segment received no benefit. Others commented that a segment should not be included in an allocation base if it received only negligible benefit. The June 30, 1972 proposal has been revised to accommodate these comments and to emphasize again the application of the concept of materiality.

(2) *Hierachy of allocation methods.* A number of commentators were concerned that a provision in the FEDERAL REGISTER of June 30, 1972, that costs be "* * * allocated on the basis of expenses caused by the segments, benefits received by the segments, or benefits available to the segments," did not provide adequate guidance for the selection of appropriate allocation bases. The Board believes that with the exception of centralized service functions, the allocation criteria contained in the fundamental requirement are sufficiently specific so as not to require additional guidance. The Board is persuaded, however, that it is desirable to establish more definitive criteria for the selection of an appropriate allocation base for centralized service functions. For this purpose, the Board has added in § 403.50(b) a hierarchy of allocation methods. The hierarchy is based on achieving the most realistic representation of the beneficial or casual relationship that is practical in the circumstances.

(3) *Allocation of residual expenses.* With few exceptions, commentators objected to the establishment of a single formula to allocate costs of managing the company as a whole, i.e., residual costs. Many noted that the formula, in conjunction with a broadly inclusive definition of a "segment," would produce inequitable allocations to certain segments. Most often concern was expressed that the allocations would have to be made to segments which receive little benefit from the home office, such as independent subsidiary corporations, subsidiaries in which the organization has only a minority ownership, foreign segments, and Government-owned contractor-operator (COGO) plants. Others were concerned that the formula was unduly complex to administer and that the results of its use would not be worth the effort, particularly where home office expenses are relatively minor in amount.

The most commonly suggested alternative to the formula was that the Standard should provide "criteria" for allocation, rather than a specific method or procedure. Some suggested, for example, that the Standard require only that the allocation base be representative of the activity of the segments. Most often the recommended criteria were phrased in such general terms as equity, fairness, and reasonableness. Some suggested total cost input, cost of sales, revenue, payroll, number of employees, or value-added, as a single allocation base.

The Board recognizes that where residual expenses are minor in amount in relation to a contractor's total business volume, the use of other techniques is unlikely to affect materially the amount allocated to a given segment, and is even less likely to affect materially the allocations to individual contracts. The Board has therefore provided in § 403.40(c) that, where residual expenses are no greater than a specified percentage of the organizations, operating revenue, they may be allocated by means of any appropriate allocation technique. To develop the percentages specified in the Standard, the Board considered both actual statistics of various companies and the results of a staff study to determine the effect of the Standard on the home office allocations of a number of companies. The choice of an alternative technique for allocation of residual expenses is expected to be available to many contractors whose home offices perform relatively few functions, or which adequately employ direct allocation or allocations by means of other homogeneous expense pools.

The Board has concluded that where residual expenses are material in amount, a single allocation technique should be specified. Accordingly, § 403.40(c) of the Standard requires the use of the three-factor formula if residual expenses are in excess of the specified percentage of total company revenues. If residual expenses are material in amount, the Board believes that selection of a single allocation technique is necessary to reduce costly controversy in an area where disputes have been commonplace. Furthermore, the Board is of the view that the greater the amount of residual expenses, the greater the likelihood that the use of a single factor base for all contractors could result in inequitable allocations. The use of the three factors in the formula minimizes any distortion that may result from any one of the factors.

The three-factor formula is selected because it takes into account the major subjects of management concern, i.e., volume or activity, employees, and invested capital. Some companies consider that the time, effort, and attention of top management attributable to various segments are approximately proportionate to the volume or activity of those segments. Revenue is considered by some companies to be a generally reliable and convenient measure of volume or activity. Other companies believe that top management efforts are primarily devoted to the employees of an organization and, therefore, advocate the use of payroll for allocating the cost of these efforts. Still others believe that a major top management concern is the management and deployment of the capital invested in the organization: for the purpose of this formula, the net book value of tangible capital assets and inventories is considered by the Board to be a reasonable representation of invested capital.

(4) *The formula factors.* In addition to permitting an alternative to the three-factor formula for allocating residual expenses, the Board has made certain modifications to the formula itself.

A number of commentators opposed the inclusion of intraorganizational sales, in the revenue factor. Several of these commentators were concerned that this procedure would "pyramid" the allocation of home office expenses to those products which progress through several segments of an organization before they are finally sold to outside customers. Others noted that a segment established primarily to sell products produced by other segments would receive a disproportionately large share of home office expenses under the formula. However, a segment which sells much or all of its output to other segments would receive a disproportionately small allocation of home office expenses if such sales were excluded from the revenue factor. The Board, therefore, has concluded that the operating revenue of a segment shall include sales to other segments, but such operating revenue shall be reduced by purchases from other segments. This procedure will assure an appropriate allocation to each segment, regardless of whether it sells to other segments or to outside customers while at the same time avoiding "pyramiding" of home office expenses.

As originally published in the FEDERAL REGISTER of June 30, 1972, the Standard required the inclusion of rental property in the property factor of the formula. Such property was to be valued at eight times the annual rental rates. Many commentators opposed the inflexible valuation of such property. Others believed the inclusion of rental property at all was entirely inappropriate. Questions were also raised whether, and to what extent, minor, short-term leases would have to be included. In view of these comments, the Board has concluded that tangible capital assets to be included in the formula should be those capitalized in accordance with a contractor's established practices.

The Board, however, did not adopt the recommendation of many commentators that the value of Government-furnished property be included in computing the property factor of each segment. These commentators were of the view that Government property requires as much, or more, management attention as owned property. The Board believes that such administration is mostly accomplished at the segment level, and therefore, residual expenses of the home office are not significantly related. Rather, property is included in the formula as a measure of top management's attention to invested capital.

(5) *Allocation of residual expenses to special segments.* As originally published in the FEDERAL REGISTER of June 30, 1972, the Standard would have required, as a general rule, the allocation of a proportionate share of residual expenses to all segments pur-

suant to the three factor formula. For this purpose, "segments" included domestic and foreign subsidiaries owned more than 50 percent as well as those subsidiaries owned between 20 percent and 50 percent if the home office exercised significant guidance and control.

Numerous comments were received in regard to these provisions. Commentators observed variously that the percentage of ownership is not in proportion to the benefits received from the home office, that the amount of guidance and control is not in proportion to the percentage of ownership, or that the benefits received are not in proportion to the amount of guidance and control. Some commentators noted that the absence of significant guidance and control is difficult to demonstrate. A number of commentators were particularly concerned about the resultant allocations to subsidiaries owned less than 50 percent, foreign subsidiaries, unconsolidated subsidiaries, and sales subsidiaries. Many commentators observed that subsidiaries often perform their own home office functions, that the necessary information to make the required allocation would not always be available, that subsidiaries could not always be billed for home office costs, or that such allocations would cause tax and legal problems. Various commentators recommended alternatively that allocations to subsidiaries be based on management judgment, on the degree of guidance and control, or on the basis of benefit, rather than on any ownership criteria. Others recommended variously that no allocation be made to subsidiaries owned less than 100 percent, to subsidiaries owned less than 50 percent, or to subsidiaries which are unconsolidated. Still others suggested partial allocations in various forms. One industry association recommended that allocations to subsidiaries be based on advance agreements with the Government.

Upon analysis of the comments received on this subject, the Board is persuaded that a requirement to allocate a pro rata share of residual expenses by means of the formula or other allocation base to all segments, without exception, could result in inequitable allocation in certain situations. In the opinion of the Board, this problem is not necessarily limited to subsidiary corporations, but can extend to other segments. Accordingly, the Board has provided in § 403.40(c)(3) of the Standard that, where the Contracting Officer and the contractor agree that a particular segment receives significantly more or less benefit from residual expenses than would be reflected by the allocation of such expenses pursuant to the formula or other representative base, they may agree to establishing a special allocation of residual expenses to such segment. Any such special allocation must reasonably reflect the benefits received by the segment. Guidance to implement this provision is contained in a new paragraph (d) under § 403.50 of the Standard.

(6) *GOCO's.* Some commentators urged that GOCO facilities be excluded from the definition of segments to receive allocations of home office expenses, arguing that the GOCO facilities receive little or no benefits from home office activities. Several commentators were concerned that this Standard would result in contractors being required to make greater allocations to GOCO's than would be reimbursed to them under the terms of some GOCO contracts. The Board believes that contractual problems associated with the allocation of costs to a GOCO contract pursuant to this Standard, where such costs represent significantly more or less benefit than the GOCO contract actually receives, can be dealt with by agreement, as discussed in the preceding section. The Board intends to consider in the near future the pervasive question of the treatment required by relevant Federal agencies of the costs allocated in accordance with any Standard.

(7) *State and local income and franchise taxes.* The Board believes that the nature of this expense is essentially the same for all companies and that there is little justification for the observed multiplicity of allocation methods being used to allocate to segments their share of corporate State and local income taxes and franchise taxes. By means of an illustration in the FEDERAL REGISTER publication of June 30, 1972, the Board proposed the

allocation of State and local income taxes on the basis of the profit and loss of each segment and specifically requested comments on this particular illustration. Numerous comments were received. While some commentators agreed with the proposed illustration, most did not. Of those that did not, most advocated an allocation method which would allocate such taxes on the basis of the same factors used to compute a segment's share of total corporate taxable income, that generally being the percentage of payroll, sales, and property of the segment to the corporate total of each of these factors. Several commentators noted that they use different allocation bases, such as income or sales, but that these result in approximately the same allocation as one based on the same factors used to compute the tax.

After evaluating the comments, the Board continues to be of the view that the nature of this expense is essentially the same for all companies. Further, allocation of this expense on the same basis used to compute a segment's share of total corporate taxable income is, in the Board's judgment, more in accord with the concept of allocating home office expenses on the basis of the beneficial or causal relationships between such expenses and receiving segments. The Board has therefore revised the illustration for the allocation of State and local taxes to permit "any base or method which results in an allocation that equals or approximates a segment's proportionate share of the tax imposed by the jurisdiction in which the segment does business, as measured by the same factors used to determine taxable income for that jurisdiction." As a practical matter, this means that the tax for any State must be allocated only to those segments that contribute to the factors used to measure taxable income for that State. If there are several segments that do business within a State, each segment's share of that State's tax is to be measured by the proportionate contribution made by such segment to the total of the factors for that State.

(8) *Cost-benefits.* Many commentators addressed themselves to the last sentence of section 719(g) of the Act which provides that. "In promulgating such standards, the Board shall take into account the probable costs of implementation compared to the probable benefits."

The Board has not neglected its obligation and continues to measure the costs and benefits involved in implementing both proposed and promulgated standards. Its experience to date leads to the conclusion that the kind and amount of empirical data called for by some commentators is neither available nor possible of accumulation. In the final analysis, the Board must determine whether the information that has been assembled and evaluated is sufficient to enable it to make reasonable judgments.

In making this determination with respect to the present Standard, the Board gave careful consideration to the evidence bearing on the likely initial and continuing implementation costs involved, both for contractors and for affected agencies of the Government. At the same time, consideration was given to the benefits which will be achieved through simplified negotiation, administration, audit, and settlement procedures; one of the major gains of standards, to contractors and the Government alike, is the reduction in the number of costly controversies. After evaluating the Standard being promulgated today, the Board finds that the probable benefits of this Standard clearly outweigh the probable cost of implementation.

(9) *Exemptions.* A number of educational institutions requested that they be exempted from the provisions of this Standard. There appears to be no disagreement that many educational institutions have "home offices" similar in many respects to those of commercial organizations. However, the educational institutions contend that, unlike commercial organizations, they develop overhead rates for institution-wide functional activities, such as education or research, in lieu of overhead rates for organizational segments. According to these educational institutions, it would serve no purpose, therefore, to require allocation of an institution's "home office" expenses to organizational segments. In addition, a number of these commentators noted

that there are problems in defining the segments of an educational institution; e.g., whether a segment is a campus, a school, a department or some other organization.

The Board is persuaded that in the light of the present practices of educational institutions in carrying out Government contracts, little purpose would be served at this time by requiring educational institutions to adhere to a standard which prescribed criteria for allocating home office expenses to organizational segments. The Board recognizes that Office of Management and Budget Circular No. A-21, which contains the cost principles applicable to grants and contracts with educational institutions, does not presently require development of indirect cost rates for individual segments of an educational institution. Therefore, for the time being, these organizations which are subject to Office of Management and Budget Circular No. A-21 are exempted from the provisions of this Standard.

In addition, the Board is exempting State and local governments subject to Office of Management and Budget Circular No. A-87 from the provisions of this Standard pending further study of the applicability of this Standard to such organizations.

(10) *Effective date.* As originally published in the FEDERAL REGISTER of June 30, 1972, the Standard would have had to be followed by a contractor for his first fiscal year following the receipt of a contract to which the Standard is applicable. A number of commentators observed that if a contractor received a contract shortly after the effective date of the Standard and his fiscal year began shortly thereafter, little time would be available to implement the Standard. Most of these commentators requested that at least 6 months be allowed to make the necessary preparations to implement the Standard. To accommodate these requests, the Standard, now being published, requires that it must be followed for a contractor's fiscal year beginning after September 30, 1973.

(11) *Other comments.* In addition to those changes already discussed, the Board has made a number of other changes as a result of the comments received. While these are considered to be of a minor or editorial nature, the Board calls particular attention to the following additional comments.

Various commentators stated that this Standard would require contractors to accumulate and allocate home office expenses on a different basis than that used for internal management purposes. As a consequence, these commentators were concerned that the Standard would necessitate two separate sets of records. Others urged that the Standard specifically permit the use of memorandum records. The Board notes that even in the absence of this Standard, many contractors now use memorandum records to make home office allocations for purposes of Government contracts because they do not make formal allocations of home office expenses to segments, or do so on a different basis. The Board sees no need to disturb the practice of using memorandum records for home office allocations, nor does it view this as being a significant burden on contractors who find the need to do so. However, the Board does not consider it necessary or appropriate to refer specifically to the use of memorandum records by means of this Standard.

Certain commentators recommended that the Standard be specific as to the use of estimated or budgeted amounts, either for pricing purposes or for purposes of actual allocations. The use of estimates or budgets for pricing purposes or for purposes of provisional rates for cost accumulation is customary, and is not considered by the Board to require specific authority by the terms of this Standard.

There is also being published today (37 FR 26678) an amendment to Part 400, Definitions, to incorporate in that part the words and phrases defined in § 403.30 of the Standard.

PREAMBLE B

Amendments, 11-7-73

Preamble to revisions of the definitions of "home office" and "tangible capital asset," § 403.30(a)(2) and (5), and editorial amendments to §§ 403.50(c)(2) and 403.70, 38 FR

30725, Nov. 7, 1973. The document amended 4 CFR Parts 331, 351, 401, 402, and 404 as well as Part 403; material relating to those parts is omitted. It appears in the supplements to those parts.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the FEDERAL REGISTER of September 5, 1973 (38 FR 23971). The amendments: * * * (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various Parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1972.

PREAMBLE C

Amendments, 8-4-75

This publication, 40 FR 32747, August 4, 1975, revised § 403.70(a) and made several amendments to Part 351. Only those portions of the preamble which describe the revision of § 403.70(a) are printed here, although the complete preamble appears as preamble F of the supplement to Part 351. A correction to the language which amended § 403.70 was printed at 40 FR 33819, August 12, 1975.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations and Part 403, Allocation of Home Office Expenses to Segments. A proposed modification to Part 351 was published in the FEDERAL REGISTER of April 3, 1975 (40 FR 14942). Twenty-seven sets of comments were received in response to that publication. After considering those comments, the most significant of which are discussed below, the Board is today publishing an amendment to its rules relative to the requirement for the submission of Disclosure Statements by defense contractors and subcontractors.

* * * * *

6. *Applicability of CAS 403.* A number of commentators noted that the April 3 proposal deleted paragraph 351.41 of the Board's regulations. This paragraph restated the requirement that only companies that met the Disclosure Statement filing requirement for Federal fiscal year 1971 were required to comply with CAS 403, *Allocation of Home Office Expenses to Segments.* These commentators asked that the Board's position be clarified as to whether or not any current revision to the Disclosure Statement requirement also changed the coverage of CAS 403. It was not the Board's intention to broaden the coverage of CAS 403 at this time. The possibility of extending the coverage of that Standard is the subject of a separate study currently underway. To make the Board's intention wholly clear, § 403.70 of CAS 403 is being revised to state explicitly rather than by cross reference the continuing coverage of that Standard. This revision has no substantive significance whatever, but instead merely sets out specifically what was and continues to be the exemption from that Standard, which was before today accomplished by reference to § 351.40 of the Board's Basic Requirements. Contractors and subcontractors which together with their subsidiaries did not receive net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaling more than $30 million continue to be exempt from Standard 403.

PREAMBLE D

Amendment Published 9-12-77

This document amended § 403.70(a) and designated the existing text of § 403.80 as (a) and added (b). The amendment was published at 42 FR 45625, Sept. 12, 1977, as a part of the publication which added Part 332 and amendments to Parts 331 and 351 of this title. The complete preamble appears on the supplement to Part 332.

COMMENTS ON PART 403

With respect to the amendment of Part 403, the November 30, 1976 proposal was to revise that Standard to make it applicable to any contract which was subject to Cost Accounting Standards generally. The amendment being promulgated today retains this concept. However, as recommended by a number of commentators, the Board deferred the promulgation of this amendment pending the amendments to Parts 331 and 351 and the addition of Part 332 discussed above.

The decision to extend the application of Part 403 to additional contractors was made on the basis of extensive research. This research included both those contractors who were already required to use Part 403 and those who were expected to use it as a result of this amendment. With respect to the current users, the Board is satisfied that this Standard has resulted in more equitable allocations, with little administrative effort in most cases. With respect to potential additional users, the research indicated that many of these would have to make few, if any, changes to comply with Part 403 and that the remainder could comply with little difficulty. The Board notes in addition, an independent study by the Conference Board which found that defense contractors who are using Part 403 for contract costing purposes are using the same allocation procedures for internal reporting purposes. According to the Conference Board it was typical of these companies to allocate home office expenses on a blanket basis prior to the promulgation of Part 403. (Information Bulletin No. 17, February 1977.)

A number of commentators suggested various limitations for the application of Part 403. Some of these suggestions were expressed in general terms. Some of the commentators recommended, for example, that the requirement to use Part 403 should not be extended to "small contractors." Alternatively or additionally it was recommended that Part 403 should not be required for a large contractor with little work subject to Cost Accounting Standards. More specifically, recommendations were received to exempt those contractors with less than 10 percent of their revenue from Government work. Others recommended that contractors who have less than $10 million in contracts subject to Cost Accounting Standards should be exempt. The Board believes that the recommendations of this nature have been accommodated to the extent desirable and practical by the amendments to Parts 331 and 351 and the addition of Part 332 being promulgated today. Accordingly, any further exemption from Part 403, specifically, is considered to be necessary.

In publishing the proposed amendment to Part 403 in the FEDERAL REGISTER of November 30, 1976, the Board stated that there is evidence that almost all contractors who were required to make significant changes in their allocation practices as a result of Part 403 did so without undue trouble or expense. Several commentators questioned the Board's conclusion in this regard. The Board's conclusion was based in part on Staff research involving 147 home offices who now use Part 403 to allocate home office expenses. This research sought to determine, among other things, the administrative problems and expense involved in making allocations pursuant to Part 403. Government auditors reported that of the 147 home offices, only 4 had problems in developing the necessary data and that there was evidence of significant administrative costs at one of these four offices. In addition, evidence of significant administrative costs in making the allocations was found by the Government auditors at four other of the 147 home offices.

Some of the respondents who questioned the Board's conclusions regarding administrative problems and expense referred to an industry report on the economic impact of Cost Accounting Standards as support for this position. These respondents variously referred the Board to those sections of the report which summarized (i) contractor's appraisal of benefits from Part 403; (ii) the number of contractors who were required to make changes as a result of Part 403; (iii) the number of noncompliance notices issued in connection with Part 403; and (iv) the increase and decrease in costs allocated to Government work as a result of CAS 403. Nothing in these sections, however, specifically addresses the question of administrative problems or expense involved in complying with Part 403.

Two associations reported that, contrary to the Board's findings, their member companies had experienced trouble and expense in complying with Part 403. These associations declined to identify the companies involved, the nature of the problems, or the amount of the expenses. Under these circumstances, there is no basis to alter the conclusion that contractors have been able to make changes required as a result of Part 403 without undue trouble or expense.

One commentator stated that it would not be desirable to make more contractors subject to Part 403 because he believes it to be defective, particularly with respect to its application to the allocation of state and local taxes. With respect to the application of the Standard to the allocation of state and local taxes specifically, the Board notes that it reached its conclusion on the basis of considerable research and extensive deliberation. Moreover, it has reexamined its conclusion, even after the promulgation of Part 403. Notwithstanding the views of the commentator, the Board continues of the view that the provision in question is proper. Accordingly, the Board does not agree that this Standard should not be extended to additional contractors because of the tax allocation provision.

EFFECTIVE DATE

The effective date of the regulations being published today is March 10, 1978. Pub. L. 91-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

PREAMBLE E

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 403.10 and 403.70(b). This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to §§ 403.10 and 403.70(b) are printed here. The remainder of the preamble appears as preamble K of the supplement of Part 331.

* * * * *

In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No. comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 404—CAPITALIZATION OF TANGIBLE ASSETS

Sec.

404.10 General applicability.
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PREAMBLES A—D

AUTHORITY: 84 Stat. 796, sec. 103, 50 U.S.C. App. 2168.

SOURCE: 38 FR 5321, Feb. 27, 1973, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (38 FR 5318, February 27, 1973) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 404.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

PREAMBLES: For preamble to § 404.10, see preamble C of the supplement to this part. For preamble to superseded regulations see Preamble A of the supplement.

§ 404.20 Purpose.

This Standard requires that, for purposes of cost measurement, contractors establish and adhere to policies with respect to capitalization of tangible assets which satisfy criteria set forth herein. Normally, cost measurements are based on the concept of enterprise continuity; this concept implies that major asset acquisitions will be capitalized, so that the cost applicable to current and future accounting periods can be allocated to cost objectives of those periods. A capitalization policy in accordance with this Standard will facilitate measurement of costs consistently over time.

§ 404.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Asset accountability unit.* A tangible capital asset which is a component of plant and equipment that is capitalized when acquired or whose replacement is capitalized when the unit is removed, transferred, sold, abandoned, demolished, or otherwise disposed of.

(2) *Original complement of low cost equipment.* A group of items acquired for the initial outfitting of a tangible capital asset or an operational unit, or a new addition to either. The items in the group individually cost less than the minimum amount established by the contractor for capitalization for the classes of assets acquired but in the aggregate they represent a material investment. The group, as a complement, is expected to be held for continued service beyond the current period. Initial outfitting of the unit is completed when the unit is ready and available for normal operations.

(3) *Repairs and maintenance.* Maintenance is the regularly recurring activity of keeping assets in normal or expected operating condition. Repair is the activity of putting them back into normal or expected operating condition. The total endeavor to obtain the expected service during the life of tangible capital assets is generally called repairs and maintenance.

(4) *Tangible capital asset.* An asset that has physical substance, more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the service it yields.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

[37 FR 4173, Feb. 29, 1972, as amended at 38 FR 30730, Nov. 7, 1973]

PREAMBLES: For preambles to amendments to § 404.30, see preambles A and B of the supplement to this part.

§ 404.40 Fundamental requirement.

(a) The acquisition cost of tangible capital assets shall be capitalized. Capitalization shall be based upon a written policy that is reasonable and consistently applied.

(b) The contractor's policy shall designate economic and physical characteristics for capitalization of tangible assets.

(1) The contractor's policy shall designate a minimum service life criterion, which shall not exceed 2 years, but which may be a shorter period. The policy shall also designate a mini-

mum acquisition cost criterion which shall not exceed $1,000, but which may be a smaller amount.

(2) The contractor's policy may designate other specific characteristics which are pertinent to his capitalization policy decisions (e.g., class of asset, physical size, identifiability and controllability, the extent of integration or independence of constituent units).

(3) The contractor's policy shall provide for identification of asset accountability units to the maximum extent practical.

(4) The contractor's policy may designate higher minimum dollar limitations for original complement of low cost equipment and for betterments and improvements than the limitation established in accordance with paragraph (b)(1) of this section, provided such higher limitations are reasonable in the contractor's circumstances.

(c) Tangible assets shall be capitalized when both of the criteria in the contractor's policy as required in paragraph (b)(1) of this section are met, except that assets described in paragraph (b)(4) of this section shall be capitalized in accordance with the criteria established in accordance with that paragraph.

(d) Costs incurred subsequent to the acquisition of a tangible capital asset which result in extending the life or increasing the productivity of that asset (e.g., betterments and improvements) and which meet the contractor's established criteria for capitalization shall be capitalized with appropriate accounting for replaced asset accountability units. However, costs incurred for repairs and maintenance to a tangible capital asset which either restore the asset to, or maintain it at, its normal or expected service life or production capacity shall be treated as costs of the current period.

[38 FR 5321, Feb. 27, 1973, as amended at 45 FR 13723, Mar. 3, 1980]

Preamble: For preamble affecting § 404.40, see preamble D of the supplement to this part.

§ 404.50 Techniques for application.

(a) The cost to acquire a tangible capital asset includes the purchase price of the asset and costs necessary to prepare the asset for use.

(1) The purchase price of an asset shall be adjusted to the extent practical by premiums and extra charges paid or discounts and credits received which properly reflect an adjustment in the purchase price.

(i) Purchase price is the consideration given in exchange for an asset and is determined by cash paid, or to the extent payment is not made in cash, in an amount equivalent to what would be the cash price basis. Where this amount is not available, the purchase price is determined by the current value of the consideration given in exchange for the asset. For example, current value for a credit instrument is the amount immediately required to settle the obligation or the amount of money which might have been raised directly through the use of the same instrument employed in making the credit purchase. The current value of an equity security is its market value. Market value is the current or prevailing price of the security as indicated by recent market quotations. If such values are unavailable or not appropriate (thin market, volatile price movement, etc.), an acceptable alternative is the fair value of the asset acquired.

(ii) Donated assets which, at the time of receipt, meet the contractor's criteria for capitalization shall be capitalized at their fair value at that time.

(2) Costs necessary to prepare the asset for use include the cost of placing the asset in location and bringing the asset to a condition necessary for normal or expected use. Where material in amount, such costs, including initial inspection and testing, installation and similar expenses, shall be capitalized.

(b) Tangible capital assets constructed or fabricated by a contractor for its own use shall be capitalized at amounts which include all indirect costs properly allocable to such assets. This requires the capitalization of general and administrative expenses when such expenses are identifiable with the constructed asset and are material in amount (e.g., when the in-house construction effort requires planning, supervisory, or other significant effort by officers or other personnel whose salaries are regularly charged to general and administrative expenses). When the constructed assets are identical with or similar to the contractor's regular product, such assets shall be capitalized at amounts which include a full share of indirect costs.

(c) In circumstances where the acquisition by purchase or donation of previously used tangible capital assets is not an arm's length transaction, acquisition cost shall be limited to the capitalized cost of the asset to the owner who last acquired the asset through an arm's-length transaction, reduced by depreciation charges from date of that acquisition to date of gift or sale.

(d) Under the "purchase method" of accounting for business combinations, acquired tangible capital assets shall be assigned a portion of the cost of the acquired company, not to exceed their fair value at date of acquisition. Where the fair value of identifiable acquired assets less liabilities assumed exceeds the purchase price of the acquired company in an acquisition under the "purchase method," the value otherwise assignable to tangible capital assets shall be reduced by a proportionate part of the excess.

(e) Under the "pooling of interest method" of accounting for business combinations, the values established for tangible capital assets for financial accounting shall be the values used for determining the cost of such assets.

(f) Asset accountability units shall be identified and separately capitalized at the time the assets are acquired. However, whether or not the contractor identifies and separately capitalizes a unit initially, the contractor shall remove the unit from the asset accounts when it is disposed of and, if replaced, its replacement shall be capitalized.

§ 404.60 Illustrations.

(a) *Illustrations of costs which must be capitalized.* (1) Contractor has an established policy of capitalizing tangible assets which have a service life of more than 1 year and a cost of $2,000. The contractor's policy must be modified to conform to the $1,000 policy limitation on minimum acquisition cost established by the Standard.

(i) Contractor acquires a tangible capital asset with a life of 18 months at a cost of $1,200. The Standard requires that the asset be capitalized in compliance with contractor's policy as to service life.

(ii) Contractor acquires a tangible asset with a life of 18 months at a cost of $900. The asset need not be capitalized unless the contractor's revised policy establishes a minimum cost criterion below $900.

(2) Contractor has an established policy of capitalizing tangible assets which have a service life of more than 1 year and a cost of $250. The Standard requires that, based upon contractor's policy, the asset be capitalized.

(3) Contractor establishes a major new production facility. In the process, a number of large and small items of equipment were acquired to outfit it. The contractor has an established policy of capitalizing individual items of tangible assets which have a service life of over 1 year and a cost of $500, and all items meeting these requirements were capitalized. In addition, the contractor's policy requires capitalization of an original complement which has a service life of over 1 year and a cost of $5,000. Items of durable equipment acquired for the production facility costing less than $500 each aggregated $50,000. Based upon the contractor's policy, the durable equipment items must be capitalized as the original complement of low cost equipment. (The concept of original complement applies to such items as books in a new library, impact wrenches in a new factory, work benches and racks in a new production facility, or furniture and fixtures in a new office building.)

(4) Contractor has an established policy for treating its heavy presses and their power supplies as separate asset accountability units. A power supply is replaced during the service life of the related press. The Standard requires that, based upon the contractor's policy, the new power supply be capitalized with appropriate accounting for the replaced unit.

(b) *Illustrations of costs which need not be capitalized.* (1) The contractor has an established policy of capitalizing tangible assets which have a service life of 2 years and a cost of $500. The contractor acquires an asset with a useful life of 18 months and a cost of $5,000. The tangible asset should be expensed because it does not meet the 2 year criterion.

(2) The contractor establishes a new assembly line. In outfitting the line, the contractor acquires $5,000 of small tools. On similar assembly lines under similar conditions, the original complement of small tools was expensed because the complement was replaced annually as a result of loss, pilferage, breakage, and physical wear and tear. Because the unit of original complement does not meet the contractor's service life criterion for capitalization (1 year), the small tools may be expensed.

[38 FR 5321, Feb. 27, 1973, as amended at 45 FR 13723, Mar. 3, 1980]

PREAMBLE: For preamble affecting § 404.60, see preamble D of the supplement to this part.

§ 404.70 Exemptions.

None for this Standard.

§ 404.80 Effective date.

(a) The effective date of this standard is July 1, 1973. The standard shall be applied to accrued expenditures for acquisition of tangible capital assets during the contractor's next fiscal year beginning on or after October 1, 1973.

(b) Sections 404.40(b)(1), 404.60(a)(1), and 404.60(a)(2), as amended, shall be applied to accrued expenditures for acquisition of tangible capital assets during the contractor's cost accounting periods which begin on or after December 20, 1980.

[38 FR 12319, May 5, 1973, as amended at 45 FR 13723, Mar. 3, 1980]

PREAMBLES: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined. For other preambles affecting § 404.80, see preamble D of the supplement to this part.

PREAMBLE A

Preamble to Original Publication of Part 404, 12-27-73

Preamble, published at 38 FR 5318, Feb. 27, 1973, to the original publication of this part.

The Standard on Capitalization of Tangible Assets published today is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. app. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Standard was initiated as the result of recognition that the general subject of fixed asset accounting has been the source of continuing problems between contractors and the Government concerning equitable determinations of the costs attributable to performance of specific contracts. The problems include (1) determination of the acquisition costs to be capitalized as opposed to those which are charged against revenues of the current period, (2) determination of appropriate depreciation charges for a given fiscal period, (3) determination of the appropriate allocation of depreciation charges among contractor activities, and (4) determination of appropriate techniques for treating dispositions of fixed assets. The Standard establishes the beginning point for fixed asset accounting as described in (1) above. It does not cover the other related topics.

Early research on this Standard included an extensive review of available literature on the subject and a review of decisions of contract appeals boards and courts. A preliminary analysis of the entire topic of fixed asset accounting was made and a number of issues were identified; comments on this analysis were obtained in response to an extensive mailing. After careful evaluation of the comments, the Board developed and circulated a questionnaire on tangible fixed asset accounting practices. The replies to the questionnaire were considered in the preparation of a preliminary draft of the Standard on Capitalization of Tangible Assets, which was, in turn, widely distributed for informal comment by interested parties.

The Standard now being promulgated is derived from the proposal which was published in the FEDERAL REGISTER for October 5, 1972, with an invitation for interested parties to submit data, views, and arguments to the Board. The Board supplemented that FEDERAL REGISTER publication by sending copies of the FEDERAL REGISTER material directly to organizations and individuals who were expected to be interested. Responses were received from 107 sources, including individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. All of the comments have been carefully considered by the Board.

Most of those who commented expressed general concurrence with the provisions of the proposal. Many of the contractors who commented indicated that their practices in most respects already complied with the Standard; most suggested that the proposal should be modified only in a few respects. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. Many companies and individuals have devoted significant talent and effort to the improvement of this Standard.

The comments below summarize the major issues discussed in connection with the October 5 proposal and explain the major changes which have been made.

(1) *Adequacy of existing situation.* Some commentators contended that the Board should not promulgate any rules in this area because the applicable principles have been well established and accepted. The Board, however, finds that the existing regulations have failed to establish reasonable uniformity of capitalization practices among comparable organizations.

(2) *Specificity.* Some interested parties criticized the proposed Standard on the basis that it was "too procedural." Those who comment in this vein tend to assert that this Cost Accounting Standard should deal only with criteria and policies. Others criticized the October 5 proposal as being too general and failing to provide sufficient guidance about treatment of specific types of costs (such as sales tax) or certain types of transactions (such as deferred maintenance).

The Standard provides practical implementation for the basic concept of direct identification of costs with final cost objectives to the maximum practical extent. The acquisition costs of tangible assets should be identified and capitalized wherever the service lives and amounts involved are so significant that contract costs would be distorted if the acquisition costs were not capitalized. The main feature of this Standard is the requirement that contractors consistently apply reasonable capitalization policies in accordance with criteria stated in the Standard.

A policy for capitalization is a policy for distinguishing between assets and expenses. Immediate charge-off is justifiable as a practical expedient in those situations where the improved allocation of cost among cost objectives and accounting periods which would be attainable by capitalization is worth the administrative costs which would be required. Assets with either short service lives or minor acquisition costs are conveniently accounted for as charges against current revenues.

When a transaction is identified as the acquisition of a tangible capital asset, the full cost of acquiring the asset should be capitalized. The Board might have applied this concept by requiring the inclusion of specific elements of cost in the determination of acquisition cost. As one example, it would be appropriate in concept to capitalize sales and use taxes as a part of the acquisition cost because such taxes are clearly caused by the acquisition. However, as many commentators have stated, as requirement to capitalize such taxes and similar costs would require significant changes in contractor's accounting systems and the benefit from such increased uniformity may not exceed the expected cost to contractors if required to change from their present practices. The Standard, therefore, does not specifically require the capitalization of sales or use taxes or other collateral costs of acquiring tangible capital assets. The subject remains under active consideration by the Board and if further study should indicate that the benefits from increased uniformity in this area would outweigh probable administrative costs, the Board will take affirmative action on this subject.

This Standard does not provide procedural detail for determining the accounting treatment for some specific kinds of transactions related to existing assets. The major problems encountered in practice are those of classification; once specific work is defined, for example, as "preventive maintenance," "routine repair," "major overhaul," "extensive renovation," "addition," "betterment," or some other such classification in accordance with contractor policy, the appropriate accounting treatment can readily be agreed upon.

The Standard leaves latitude to the contractor in establishing his capitalization policy, but it provides some reasonable limits. A major purpose of Cost Accounting Standards is increased uniformity and consistency; this goal implies some reduction in the flexibility which was formerly available.

(3) *Capitalization as an independent issue.* As indicated above, the research which has led to this Standard began as a broad inquiry into a number of closely related issues. Capitalization is only one of those issues. Interested parties have suggested that the Board should not issue a Standard on any single part of the subject of fixed asset accounting until it is prepared to deal comprehensively with all related issues. The major objection is that changes in this Standard may be found to be appropriate when the details of a Standard on depreciation are agreed upon.

After careful consideration of all issues presented, the Board is confident that the Standard being promulgated will be compatible with future Standards. Nonetheless the Board acknowledges that because of future Standards, or for other reasons, modification in this, or indeed in any Standard which it promulgates, may be necessary. Should such modifications be needed, they will be made. This Standard, by helping identify those acquisitions which should be capitalized, will be useful immediately in connection with identifying items whose cost should not be allocated to current contracts.

(4) *Definition of tangible capital asset.* The term "Tangible Capital Asset" has already been defined by the Board in connection with the Cost Accounting Standard on Allocation of Home Office Expenses to Segments. The definition provides that such assets "are to be held for continued use or possession * * * for the services they yield." Some interested parties have suggested that this definition could apply to inventories which are held for sale. The Board considers that the phrase "for the services they yield" is sufficient to show that the term does not apply to inventories. No change is deemed necessary in the published definition.

(5) *Nature of limits.* The Standard requires that each contractor establish and adhere to a reasonable capitalization policy. The Board feels that, in most cases, the contractor is best able to determine what policy will be most suitable for his situation, and that all interested parties will be benefited by consistent application of appropriate criteria for distinguishing between capital items and those which should be charged off at time of acquisition. In consideration of the possible distortion and inequity which might result from application of an unreasonable policy (significant amounts of long-term fixed asset costs charged to expense at acquisition), the Board considered the desirability of a specific definition of the limits of reasonableness. The proposal published in October, as well as earlier drafts distributed informally, included the requirements that the policy deal with both the expected service life and the acquisition cost. An acceptable policy would not allow an asset to be charged off immediately against revenue if its service life was expected to be in excess of 2 years and its acquisition cost was in excess of $500.

The Board received many comments on the provision of these specific limitations. Critics have used the term "arbitrary." The Board has considered carefully all the pertinent points and has continued the limits which were earlier proposed. Disclosure statements and other research data obtained by the Board indicate that very few contractors will be required to change their present policies and those few required changes will impact only a few acquisitions. A review of disclosure statements filed with the Board indicates that only 3 percent of the reporting companies had dollar capitalization criteria in excess of $500. In addition, the fact that specific limits, appropriate today, may need to be revised in the future is not a reason to avoid establishing them today. Limitations can be revised promptly if developments warrant a change.

There have been no established limits on capitalization policies. Accordingly, wide diversity exists among contractors. The Board does not seek to establish a single uniform accounting system for all contractors, but it believes that limits for total cost and useful life should be placed under some uniform constraints. Indeed, the Board feels that procurement authorities are entitled to assurance that contractor capitalization policies will result in the capitalization of those acquired assets which are within specific limits of reasonableness.

(6) *Comparing benefits and costs.* The Congress provided, in section 719(g) of the Act which established the Board, that in promulgating Cost Accounting Standards "the Board shall take into account the probable costs of implementation compared to the probable benefits." Those commenting on the Board's work show considerable interest in this aspect; the comments on the October proposal included a number of remarks on this comparison.

The Board considers the benefits and the costs which can be related to each specific proposal and also to the total program of developing Cost Accounting Standards. This Standard has, for most contractors, almost no cost. It requires the adoption of a policy; most contractors already have policies which comply with the criteria. Some contractors, however, will have to establish or modify capitalization policies; for these contractors there may be costs. Benefits will be available immediately; contract administration will be improved. Once a capitalization policy is established in accordance with the standard, individual acquisitions can be handled in accordance with the established policy, with a reduction in controversy. This Standard establishes the beginning point for the determination of the costs associated with use of capitalized tangible assets. One of the major benefits of this Standard is, therefore, the provision of a more uniform basis on which the Government and contractors may deal with depreciation expense.

During the development process which led to this Standard, the Board asked for, and received, a number of comments from contractors about the likely costs attributable to the implementation of a proposal such as this one. Most replies indicated little or no cost. Some indicated compliance with this Standard will cause divergence from practices now accepted for other purposes. The Board has found no requirement imposed by other authoritative bodies for continuance of practices inconsistent with this Standard. Divergence, therefore, will occur only if an affected contractor elects, for other purposes, practices inconsistent with the criteria set forth in this Standard.

The Board concludes that this Standard will provide benefits which outweigh the costs of implementation.

(7) *Accounting for assets acquired by lease.* Many commentators suggested to the Board various methods of accounting for assets acquired by lease. This problem is not a new one. Tangible assets can be acquired by various kinds of business transactions and relationships. The accounting principles related to capitalization are most readily applied in connection with purchases. Some lease agreements provide to the user of an asset many of the attributes of ownership. The accounting profession has long been cognizant of difficulties related to determining

when assets acquired by lease should be treated as purchases.

The Board agrees that assets actually purchased should (if otherwise appropriate for capitalization) be capitalized even when the purchase transaction is in the form of a lease agreement.

This same determination must be made for other accounting purposes. The accounting profession is now guided, in this regard, primarily by opinions of the Accounting Principles Board; it is our understanding that the Financial Accounting Standards Board will soon undertake to provide a new statement for the profession on this issue. This Board will carefully consider all authoritative statements of accounting principles to the extent that it can do so while maintaining progress toward its own primary goal of increased uniformity and consistency in cost accounting for contracts.

Those lease acquisitions which are treated as purchases will be subject to this standard; those which are treated as leases will for the time being be subject to the existing procurement regulations which deal with rental costs. The Board is, therefore, willing that the contractor determine, for each acquisition, whether it is a purchase and hence subject to his capitalization policy (which must comply with the criteria established in this Standard) or a rental transaction and hence subject to established regulations on rental costs. In either case, determination of the reasonableness of the lease costs remains the responsibility of the procurement agencies and is not dealt with here by the Cost Accounting Standards Board.

(8) *Investment Credit.* The October proposal included a specific provision that the Investment Credit pursuant to the Revenue Act of 1971, Pub. L. 92-178, need not be deducted from the purchase price of tangible capital assets in establishing the acquisition cost of the assets. Several interested parties criticized the language used in this provision. Public policy on the point is clear; the Board, by including a specific provision, did not intend to change the situation. The Investment Credit need not be deducted, and there is no need for a specific provision on this point. The Board has, therefore, removed the provision.

(9) *Indirect cost for constructed assets.* The October 5 proposal contained a provision that the acquisition costs of assets constructed or fabricated by a contractor should include the indirect costs allocable to final cost objectives. The Board specifically drew attention to this treatment of such assets and requested that anyone advocating an alternative treatment should set it forth in detail with reasons for favoring it. Numerous commentators opposed the Board's proposed treatment of constructed assets, stating variously that the allocation of general and administrative expenses to such assets was contrary to generally accepted accounting principles (since such expenses are period costs), was not required by existing Government regulations, and no one accounts for such assets in this manner. A few suggestions for alternative treatment were made. Most of them dealt with allocating to constructed assets only variable indirect costs that could be directly identified with the assets constructed.

For financial reporting purposes some indirect costs are identified as period costs and are not considered to be inventoriable. Consistent application of the full costing concept generally applicable to Government contract costing is not compatible with that period cost concept; for such contract costing, all costs—including those otherwise considered as period costs—must be associated with final cost objectives. The October 5 proposal identified constructed assets as projects which should be treated as final cost objectives and share in indirect cost allocations. This treatment is consistent with the casting practice which would be followed if the Government contracted for the construction of fabrication of the assets in question.

The Board continues to be of the view that application of the full costing techniques applicable to Government contract costing requires that full consideration be given to the applicability of fixed overhead including general and administrative expense to constructed assets. Some fixed overhead at the operations level and certain general and administrative expenses are often allocable to constructed assets based on their beneficial relationship to the construction effort. Costs generally not so allocable could include selling expenses, bid and proposal expenses, and the like.

Therefore, tangible capital assets constructed which are identical with or similar to the contractor's normal product should receive an appropriate share of all indirect cost including general and administrative expenses. In addition, other constructed tangible capital assets requiring significant indirect support also should be burdened with their allocable share of indirect costs, where such indirect costs are material. The revised § 404.50(b) reflects this position.

(10) *Grouping of assets.* The proposed standard as published October 5 was construed by a number of readers to imply that capital assets should be accounted for on a unit basis and not in groups. The Board did not intend any such implication. The Board's interest is in costing principles and the requirements to capitalize does not extend to the specific type of records to be maintained.

(11) *Rearrangement costs.* Many of the controversies related to capitalization are encountered in connection with costs incurred subsequent to the acquisition of an asset. Routine repair costs are unquestionably to be charged off against current revenues, while costs of major betterments are clearly to be capitalized. Costs which are not at either extreme are more difficult to account for. The October 5 proposal included a restatement of the principle that "costs incurred subsequent to the acquisition of a tangible capital asset for activities which extend the life or increase the usefulness of that asset (e.g., betterments) and which meet the contractor's established criteria for capitalization shall be capitalized." This aspect of the proposal was generally favored by commentators. The proposal continued with the requirement that expenditures for rearrangement and reconversion of tangible capital assets, if they extend the life or increase the usefulness of those assets, and which meet the capitalization criteria, should be capitalized. This requirement has been criticized; many contractors assert that rearrangement costs, as they use the term, should never be capitalized.

The Board agrees that rearrangements of the sort normally expected to maintain the usefulness of assets should not be capitalized. The Board expects that rearrangements of the sort which extend the life or increase the usefulness otherwise anticipated from tangible capital assets, will be classified as betterments and capitalized in accordance with the requirements of the standard. Accordingly, the term "rearrangement" has been deleted from the standard.

(12) *Special purpose equipment.* The Board has received a number of suggestions that the Standard should provide explicit coverage for special purpose assets. Consideration was given to this issue in the research which led to the October 5 proposal. "Special tooling" and "special test equipment" are defined in Government procurement regulations; expenditures of such assets are properly charged against the contracts for which their acquisition is authorized. The suggestions for modification of the October 5 proposal on this point mostly deal with acquisitions which do not qualify as "special tooling" or "special test equipment."

Contractors do acquire assets which are expected to have technological or engineering capabilities for long periods but for which the contractor does not foresee any significant utility after the completion of a particular contract. Such assets are not "special purpose" assets. Rather they are assets for which the contractor expects relatively short economic service life (as compared with the physical potential). Most suggestions for a change in the standard at this point seemed to be based on the belief that these assets should not be capitalized. The standard being promulgated today is applicable to all acquisitions; each contractor's policy is required to include appropriate criteria (e.g., estimated service life and economic usefulness) for identification of capitalizable assets, including those which are unusual.

(13) *Donated assets.* Some commentators opposed that part of the standard which requires the capitalization

of assets donated by the Government. These commentators pointed out that such treatment may eventually result in depreciation charges to Government contracts and that Government regulations today make such depreciation charges unallowable. The allowability of depreciation costs of assets donated by the Government will not be influenced by the requirement that such assets be capitalized.

(14) *Original complements of low cost equipment.* A number of interested parties were concerned with the concept of original complement. Those who commented asserted that there was an inconsistency in capitalizing items of little value, that it would be difficult to identify or control individual items, and that alternative accounting methods were used to achieve the same results of normalization of cost between periods.

The Board's primary purpose in requiring the capitalization of original complements is to assure allocation of incurred cost to applicable current and future accounting periods. The Board sees no inconsistency in this purpose.

The total original complement should be treated as a tangible capital asset. Therefore, the Board expects that a contractor will identify and control the original complement as an entity rather than account separately for each individual item which comprises the total complement.

The Board recognizes that several methods are used to distribute the cost of original complements to future accounting periods:

(1) Treating the complement as a tangible capital asset subject to depreciation, (2) treating the cost as a deferral charge, or (3) treating the original complement as an inventoriable asset. A standard on depreciation is expected to prescribe acceptable methods for charging the cost of original complements to accounting periods; the standard being promulgated today requires that the complement be capitalized.

(15) *Asset accountability unit.* A number of interested parties indicated problems with both the concept and definition of a retirement unit as published in the October proposal. The term retirement unit has been changed to "Asset Accountability Unit" which the Board believes to be more descriptive of the concept actually applied in identifying components of major assets. These units, to the maximum extent practical, should be identified and separately capitalized upon acquisition and, whether or not they have been previously separately capitalized, they should be removed from the asset accounts when disposed of. Replacement units should also be capitalized.

(16) *Application of the standard.* Several universities commented that the proposed Standard should not apply to them because universities generally do not use depreciation techniques. Under existing procurement regulations, universities are entitled to a use allowance for fixed assets in lieu of a depreciation charge. The Board believes that the Standard on Capitalization is applicable to universities and others in determining capitalized cost for computation of use allowances or similar purposes and for identifying those items which are not appropriate for current charges. Therefore, no exemptions are provided for by this Standard.

There is also being published today (38 FR 5318) and amendment to Part 400, Definitions, to incorporate in that part the words and phrases defined in § 404.30 of the Standard.

PREAMBLE B

Amendments, 11-7-73

This publication, 38 FR 30725, Nov. 7, 1973, amended § 404.30(a)(4) by revising the definition of "tangible capital assets".

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the FEDERAL REGISTER of September 5, 1973 (38 FR 23971). The amendments: (a) Renumber Parts 331 and 351 to facilitate insertion of future modifications to those parts; (b) clarify one section of the contract clause at § 331.5; and (c) modify certain definitions in Parts

400, 401, 402, 403, and 404 for the purposes of uniformity among the various Parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973.

Preamble C

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 404.10. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 404.10 is printed here. The remainder of the preamble appears as preamble K of the supplemental to Part 331.

* * * * *

In the Federal Register of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preamble D

Amendments published 3-3-80

This publication, 45 FR 13721, Mar. 3, 1980, revised § 404.40(b)(1) and § 404.80(b) and amended § 404.60(a)(1) introductory text, (a)(1)(i) and (ii).

Summary

Part 404 includes a requirement that defense contractors have written policies for capitalization of tangible assets. Each such policy must include a minimum acquisition cost criterion, which has not been allowed to exceed $500. The Standard is being amended to raise the limit to $1,000. The purpose of the change is to permit contractors to adopt practices appropriate in today's economy.

Effective Date

December 20, 1980.

Supplementary Information

(1) *Background.* The amendment being promulgated today was, in one sense, anticipated at the time the Board promulgated Cost Accounting Standard 404. In its publication of February 27, 1973 the Board commented ". . . that specific limits, appropriate today, may need to be revised in the future. . . . Limitations can be revised promptly if developments warrant a change." This amendment is a specific recognition that a change is warranted.

The amendment now being promulgated is derived directly from the proposal which was published in the Federal Register for January 2, 1980 (45 FR 48) with an invitation for interested parties to submit comments. The Board sent copies of the proposal directly to organizations who were expected to be interested. The Board received 25 letters of comment on the January 2 proposal. The Board appreciates the participation by interested parties in its continuing effort to maintain the effectiveness of its Standards and regulations.

The remarks which follow summarize the major issues discussed in the comments on the January 2 proposal.

(2) *The specific change from $500 to $1,000.* CAS 404, as promulgated in 1973, contained a requirement for a written capitalization policy. The policy was required to include a minimum acquisition cost criterion, and that criterion was not allowed to exceed $500. The $500 limitation, selected as a ceiling to prevent unreasonable policies, encompassed the practices of 97% of the companies whose Disclosure Statements were filed with the Board.

The Board, recognizing that circumstances have changed significantly since the promulgation of Standard 404, authorized an inquiry into capitalization practices. With the cooperation of the National Association of Accountants, the Board mailed a questionnaire to about 200 NAA members who were able to describe the practices of large, medium, and small manufacturing firms which had not been influenced by the limitation of Standard 404. The Financial Executives Institute also mailed a similar questionnaire to about 900 of its members and asked them to furnish information directly to the Board. The responses received by the Board indicated that capitalization practices have indeed changed since the promulgation of Standard 404. Freely adopted policies now tend to include higher monetary criteria than were common in 1973.

The Board is persuaded that the change is related to changing economic circumstances, and that a change in the acquisition cost criterion is warranted. The January 2 proposal was to change from $500 to $1,000. Those who commented on the proposal were generally in favor of the specific change which had been proposed. The amendment being promulgated is unchanged from the January 2 proposal in this regard.

(3) *Use of index techniques for future changes.* The Board received several suggestions dealing with the idea that, in considering similar revisions in future years, the Board should use index techniques. The Board considered this general idea before making the January 2 proposal. The Board had reviewed the performance of several official measures which might have been used if an index technique were to be adopted. The increases from 1972 to 1979 were from about 60% to about 80%, suggesting that if $500 was the right limit at the time Standard 404 was developed, a limit of about $800 or $900 might be appropriate at the end of 1979. The questionnaire responses included a significant number of business units using $1,000.

The Board will continue to consider the appropriateness of the $1,000 limitation now being imposed. The impact of inflation, as recorded in several official indexes, will be among the factors considered. The Board is, however, not prepared to provide for any automatic amendment of the dollar limitation in Standard 404.

(4) *Other clarifying language.* It was suggested that, while the Standard is being amended anyway, the Board could reduce possible misunderstandings by modifying the language in two places.

The fundamental requirement of the Standard calls for a written capitalization policy which designates ". . . economic and physical characteristics for capitalization of tangible assets." The suggestion was made that this provision be modified by adding a clarifying phrase so that it would read ". . . economic and physical characteristics which must be met before an item is required to be capitalized." This suggestion was made in order to emphasize that the service life and unit cost are not the only characteristics to be considered in making a capitalization decision. The basic belief behind the suggestion is valid. The Board agrees that other criteria, such as ability to maintain physical identifiability, may be appropriately included in a policy, and items which are not capitalizable because of failure to meet one of the criteria specified in the policy should not be capitalized even if the estimated service life and monetary cost are in excess of those stated in the policy. The Board believes that the existing language of § 404.40(b) is clear in this regard, and no change is considered necessary.

The Standard now provides, at § 404.40(b)(4), that ". . . higher minimum dollar limitations . . ." may be designated for betterments and for original complements. Some accountants believe that the distinction between an expenditure for "repair" and one for "betterment or improvement" can best be made by considering the relationship between the expenditure and the original cost or the replacement value of the item being rebuilt or modernized. They believe it is reasonable to propose a capitalization policy which includes a percentage criterion which will, in turn, result in a different dollar criterion in each situtation. One commentator suggested that the Board should eliminate the word "dollar," so that the amended Standard would allow the designation of ". . . higher minimum limitations. . . ." The Board has no objection to policies which are stated in percentage terms over the range of typical application. The Board, however, feels that it is quite reasonable to provide a monetary limit above which any betterment will be capitalized even if its cost is a low percentage of some other asset's cost. The Board is therefore not making the suggested change, but it does take this opportunity to recognize that a capitalization policy for betterments can quite reasonably include a sliding scale or percentage technique provided that it also includes a specific monetary limit.

(5) *Effective date.* The January 2 proposal would have applied to assets acquired in contractors' cost accounting periods which begin on or after January 10, 1981. Several commentators urged an earlier effective date. The Board always tries to allow adequate time for contract administrators to prepare for changes. This amendment does not require any action; rather it provides the possibility for action. The Board has changed the effective date to December 20, 1980. This change will make the amendment effective much sooner for many contractors while still allowing sufficient time for administrative implementation of the amendment.

(6) *Comparing Costs and Benefits.* The Board's January 2 publication included an explicit request for advice with respect to probable costs of implementation as compared with probable benefits. Only a few commentators dealt at all with this issue, and none of them in quantitative terms. All those who discussed this issue indicated that they expected benefits from the amendment, and that the benefits would outweigh any costs of implementation. No commentator objected to the proposal. The Board is persuaded that the probable benefits will exceed the probable costs of implementation.

Title 4 CFR 404, Capitalization of Tangible Assets is amended as follows:

PART 405—ACCOUNTING FOR UNALLOWABLE COSTS

Sec.
405.10 General applicability.
405.20 Purpose.
405.30 Definitions.
405.40 Fundamental requirement.
405.50 Techniques for application.
405.60 Illustrations.
405.70 Exemptions.
405.80 Effective date.

PREAMBLES A—B

AUTHORITY: 84 Stat. 796, Sec. 103 (50 U.S.C. App. 2168).

SOURCE: 38 FR 24198, Sept. 6, 1973, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (38 FR 24198, September 6, 1973) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 405.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

PREAMBLES: For preamble to § 405.10, see preamble B of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 405.20 Purpose.

(a) The purpose of this Cost Accounting Standard is to facilitate the negotiation, audit, administration and settlement of contracts by establishing guidelines covering: (1) Identification of costs specifically described as unallowable, at the time such costs first become defined or authoritatively designated as unallowable; and (2) the cost accounting treatment to be accorded such identified unallowable costs in order to promote the consistent application of sound cost accounting principles covering all incurred costs. The Standard is predicated on the proposition that costs incurred in carrying on the activities of an enterprise—regardless of the allowability of such costs under Government contracts—are allocable to the cost objectives with which they are identified on the basis of their beneficial or causal relationships.

(b) This Standard does not govern the allowability of costs. This is a function of the appropriate procurement or reviewing authority.

§ 405.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Directly associated cost.* Any cost which is generated solely as a result of the incurrence of another cost, and which would not have been incurred had the other cost not been incurred.

(2) *Expressly unallowable cost.* A particular item or type of cost which, under the express provisions of an applicable law, regulation, or contract, is specifically named and stated to be unallowable.

(3) *Indirect cost.* Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(4) *Unallowable cost.* Any cost which, under the provisions of any pertinent law, regulation, or contract, cannot be included in prices, cost reimbursements, or settlements under a Government contract to which it is allocable.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 405.40 Fundamental requirement.

(a) Costs expressly unallowable or mutually agreed to be unallowable, including costs mutually agreed to be unallowable directly associated costs, shall be identified and excluded from any billing, claim, or proposal applicable to a Government contract.

(b) Costs which specifically become designated as unallowable as a result of a written decision furnished by a contracting officer pursuant to contract disputes procedures shall be identified if included in or used in the computation of any billing, claim, or proposal applicable to a Government contract. This identification requirement applies also to any costs incurred for the same purpose under like circumstances as the costs specifically identified as unallowable under either this paragraph or paragraph (a) of this section.

(c) Costs which, in a contracting officer's written decision furnished pursuant to contract disputes procedures, are designated as unallowable directly associated costs of unallowable costs covered by either paragraph (a) or (b) of this section shall be accorded the identification required by paragraph (b) of this section.

(d) The costs of any work project not contractually authorized, whether or not related to performance of a proposed or existing contract, shall be accounted for, to the extent appropriate, in a manner which permits ready separation from the costs of authorized work projects.

(e) All unallowable costs covered by paragraphs (a) through (d) of this section shall be subject to the same cost accounting principles governing cost allocability as allowable costs. In circumstances where these unallowable costs normally would be part of a regular indirect-cost allocation base or bases, they shall remain in such base or bases. Where a directly associated cost is part of a category of costs normally included in an indirect-cost pool that will be allocated over a base containing the unallowable cost with which it is associated, such a directly associated cost shall be retained in the indirect-cost pool and be allocated through the regular allocation process.

(f) Where the total of the allocable and otherwise allowable costs exceeds a limitation-of-cost or ceiling-price provision in a contract, full direct and indirect cost allocation shall be made to the contract cost objective, in accordance with established cost accounting practices and Standards which regularly govern a given entity's allocations to Government contract cost objectives. In any determination of unallowable cost overrun, the amount thereof shall be identified in terms of the excess of allowable costs over the ceiling amount, rather than through specific identification of particular cost items or cost elements.

§ 405.50 Techniques for application.

(a) The detail and depth of records required as backup support for proposals, billings, or claims shall be that which is adequate to establish and maintain visibility of identified unallowable costs (including directly associated costs), their accounting status in terms of their allocability to contract cost objectives, and the cost accounting treatment which has been accorded such costs. Adherence to this cost accounting principle does not require that allocation of unallowable costs to final cost objectives be made in the detailed cost accounting records. It does require that unallowable costs be given appropriate consideration in any cost accounting determinations governing the content of allocation bases used for distributing indirect costs to cost objectives. Unallowable costs involved in the determination of rates used for standard costs, or for indirect-cost bidding or billing, need be identified only at the time rates are proposed, established, revised or adjusted.

(b) The visibility requirement of paragraph (a) of this section, may be satisfied by any form of cost identification which is adequate for purposes of contract cost determination and verification. The Standard does not require such cost identification for purposes which are not relevant to the determination of Government contract cost. Thus, to provide visibility for incurred costs, acceptable alternative practices would include: (1) The segregation of unallowable costs in separate accounts maintained for this purpose in the regular books of account; (2) the development and maintenance of separate accounting records or workpapers; or (3) the use of any less formal cost accounting techniques which establishes and maintains adequate cost identification to permit audit verification of the accounting recognition given unallowable costs. Contractors may satisfy the visibility requirements for estimated costs either: (1) By designation and description (in backup data, workpapers, etc.) of the amounts and types of any unallowable costs which have specifically been identified and recognized in making the estimates; or (2) by description of any other estimating technique employed to provide appropriate recognition of any unallowable costs pertinent to the estimates.

(c) Specific identification of unallowable costs is not required in circumstances where, based upon considerations of materiality, the Government and the contractor reach agreement on an alternate method that satisfies the purpose of the Standard.

§ 405.60 Illustrations.

(a) An auditor recommends disallowance of certain direct labor and direct material costs, for which a billing has been submitted under a contract, on the basis that these particular costs were not required for performance and were not authorized by the contract. The contracting officer issues a written decision which supports the auditor's position that the questioned costs are unallowable. Following receipt of the contracting officer's decision, the contractor must clearly identify the disallowed direct labor and direct material costs in his accounting records and reports covering any subsequent submission which includes such costs. Also, if the contractor's base for allocation of any indirect cost pool relevant to the subject contract consists of direct labor, direct material, total prime cost, total cost input, etc., he must include the disallowed direct labor and material costs in his allocation base for such pool. Had the contracting officer's decision been against the auditor, the contractor would not, of course, have been required to account separately for the costs questioned by the auditor.

(b) A contractor incurs, and separately identifies, as a part of his manufacturing overhead, certain costs which are expressly unallowable under the existing and currently effective regulations. If manufacturing overhead is regularly a part of the contractor's base for allocation of general and administrative (G&A) or other indirect expenses, the contractor must allocate the G&A or other indirect expenses to contracts and other final cost objectives by means of a base which includes the identified unallowable manufacturing overhead costs.

(c) An auditor recommends disallowance of the total direct indirect costs attributable to an organizational planning activity. The contractor claims that the total of these activity costs are allowable under the Armed Services Procurement Regulation as "Economic Planning Costs" (ASPR 15-205.47); the auditor contends that they constitute "Organization Costs" (ASPR 15-205.23) and therefore are unallowable. The issue is referred to the contracting officer for resolution pursuant to the contract disputes clause. The contracting officer issues a written decision supporting the auditor's position that the total costs questioned are unallowable under the Regulation. Following receipt of the contracting officer's decision, the contractor must identify the disallowed costs and specific other costs incurred for the same purpose in like circumstances in any subsequent estimating, cost accumulation or reporting for Government contracts, in which such costs are included. If the contracting officer's decision had supported the contractor's contention, the costs questioned by the auditor would have been allowable "Economic Planning Costs," and the contractor would not have been required to provide special identification.

(d) A defense contractor was engaged in a program of expansion and diversification of corporate activities. This involved internal corporate reorganization, as well as mergers and acquisitions. All costs of this activity were charged by the contractor as corporate or segment general and administrative (G&A) expense. In the contractor's proposals for final Segment G&A rates (including corporate home office allocations) to be applied in determining allowable costs of its defense contracts subject to section XV, Part 2, of the Armed Services Procurement Regulation, the contractor identified and excluded the expressly unallowable costs (as listed in ASPR 15-205.23) incurred for incorporation fees and for charges for special services of outside attorneys, accountants, promoters, and consultants. In addition, during the course of negotiation of interim bidding and billing G&A rates, the contractor agreed to classify as unallowable various in-house costs incurred for the expansion program, and various directly associated costs of the identifiable unallowable costs. On the basis of negotiations and agreements between the contractor and the contracting officers' authorized representatives, interim G&A rates were established, based on the net balance of allowable G&A costs. Application of the rates negotiated to proposals, and on an interim basis to billings, for covered contracts constitutes compliance with the Standard.

(e) An official of a company, whose salary, travel, and subsistence expenses are charged regularly as general and administrative (G&A) expenses, takes several business associates on what is clearly a business entertainment trip. The entertainment costs of such trips is expressly unallowable because it constitutes entertainment expense, and is separately identified by the contractor. The contractor does not regularly include his G&A expenses in any indirect-expense allocation base. In these circumstances, the official's travel and subsistence expenses would be directly associated costs for identification with the unallowable entertainment expense. However, unless this type of activity constituted a significant part of the official's regular duties and responsibilities on which his salary was based, no part of the official's salary would be required to be identified as a directly associated cost of the unallowable entertainment expense.

§ 405.70 Exemptions.

None for this Standard.

§ 405.80 Effective date.

April 1, 1974.

[38 FR 31813, Nov. 19, 1973]

PREAMBLE: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined.

PREAMBLE A

Preamble to Original Publication, 9-6-73

Preamble to the original publication of Part 405, Sept. 6, 1973, at 38 FR 24195.

The Standard on Accounting for Unallowable Costs is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub. L. 91-379, 50 U.S.C. app. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Standard was started as a result of recognition of the continuing problem concerning the accounting treatment of unallowable contract costs. There has been a lack of uniformity or comparability in the cost accounting treatment accorded unallowable costs after specific determination of their unallowability. There have also been reported problems concerning the content of indirect-cost allocation bases where unallowable costs are involved. Further, there have been instances reported of inclusion of unallowable costs in the base for progress payment billings.

There is no present requirement in agency regulations for contractor identification of unallowable costs. As a result, reports prepared by Government auditors contain frequent references to costs which are known to be unallowable but disclosed only through an audit. The Board has concluded that the identification of costs determined to be unallowable should be the subject of a Cost Accounting Standard.

This Standard requires the identification of specific costs at the time such costs first become defined or authoritatively designated as unallowable. The Standard also establishes guidelines for the cost accounting treatment to be accorded such identified costs. The Board believes that application of this Standard will provide a greater degree of uniformity in the determination of costs of negotiated defense contracts.

Early research on this Standard included a review of available literature on the subject, a review of the decisions of contract appeals boards and courts, and meetings with contractors and other organizations and individuals concerning their operations and philosophy relative to the treatment of unallowable costs.

This research led to the publication of a proposed Cost Accounting Standard in the FEDERAL REGISTER of March 30, 1973, with an invitation for interested parties to submit written data, views, and comments to the Board. To assure that those who had already expressed interest in the proposed Standard had an opportunity to comment, the Board supplemented the FEDERAL REGISTER notice by sending copies of the published material directly to several hundred organizations and individuals.

Responses were received from 67 sources, consisting of individual companies, Government agencies, professional associations, industry associations, public accounting firms and others. All of these comments have been carefully considered by the Board. Those comments which are of particular significance are discussed below, together with an explanation of the changes made to the proposed Standard published in the FEDERAL REGISTER of March 30, 1973.

Government commentators generally regarded a requirement for identification of unallowable costs as being reasonable and desirable as long as it recognized that there is room for agency judgment relative to the allowability of individual cost elements. The reaction from industry sources was generally in opposition to a Standard on this subject. The reaction from other commentators was mixed. The Board notes that in the comments by industry representatives are a significant number of admissions that at least some unallowable costs can be identified clearly in advance and, in fact, are so identified by many contractors.

The Board has greatly benefited from the many comments it received on the Standard as published in the FEDERAL REGISTER of March 30, 1973. The Board takes this opportunity to express its appreciation for the suggestions it has received, and for the time devoted to assisting the Board in this endeavor by the many companies and individuals involved.

1. *General—Need for a Standard.* Those who took specific exception to the need for or propriety of a Standard raised a number of issues. Following is a summary and discussion of each of the major issues raised:

(a) *Existing procurement regulations and procedures are adequate to resolve what is essentially an administrative issue, and are more appropriately relied upon for accomplishing the stated purposes of the Standard.*

The Board does not agree with this argument. Although the regulations of procurement agencies deal extensively with the definition of those items of cost which are not to be accepted as allowable under Government contracts, they do not require contractor identification of unallowable costs and provide only minimal guidance as to the cost accounting treatment to be accorded such costs.

The Board notes that the idea of "unallowable costs" is a concept not generally applied in commercial cost accounting, and that it apparently has no direct relevance to the process of allocating costs incurred to final cost objectives. The Board's function is to promulgate Cost Accounting Standards to "be used by all relevant Federal agencies and by defense contractors and subcontractors in estimating, accumulating, and reporting costs in connection with the pricing, administration and settlement of all negotiated prime contract and subcontract national defense procurements with the United States in excess of $100,000." The identification and measurement of unallowable costs are directly relevant to this function. In the performance of its assigned responsibility, therefore, the Board finds that a Standard establishing a concept of unallowable costs and providing for the identification, measurement, and reporting of such costs will be useful and desirable.

The Board believes that recognition of the cost accounting concept that all costs incurred in carrying on the activities of an enterprise are allocable to the cost objectives of the enterprise is essential to the maintenance of sound and consistent contract cost accounting. This is particularly significant in providing for consistent policies governing allocations of indirect costs, as discussed in greater detail in connection with the issue of indirect-cost allocation bases. It is also important in connection with the profit determinations of the Renegotiation Board, where it is necessary to determine the total costs properly allocable to renegotiable contracts. Cost Accounting Standards should result in determination of costs which are allocable to contracts and other cost objectives. The use of Cost Accounting Standards, however, has no direct bearing on allowability determinations.

(b) *The published proposal constitutes an inflexible procedural requirement rather than a cost accounting standard; it deals with minutiae and will necessitate considerable additional accounting effort and record keeping.*

The Board does not believe that a requirement for contractor identification of costs known to be unallowable, or which have clearly been designated as unallowable, represents an undue burden. It is reinforced in this belief by the fact, as stated in several of the comments received and as further shown by the Board's research, that many contractors already provide this identification, and often with a greater detail of recorded cost segregation than is required by the Standard. Revised wording has been provided to make clear the Board's intent to require only such detail and depth of cost allocation and record keeping as is necessary to provide appropriate cost visibility. Provisions for accounting recognition of unallowable costs are considered appropriate for a Standard.

The Board does not agree that this standard deals with minutiae. A significant amount of the time of both Government and contractor personnel is spent in identifying contract costs and in negotiating their allowability. The cumulative impact of unallowable costs can significantly affect contract cost reimbursement and pricing. For example, in fiscal year 1973, the Department of Defense disallowed costs exceeding $200 million. The Board believes that a Standard which will foster earlier and more precise identification of unallowable costs, and thereby narrow the areas of cost search, disagreement and negotiation of differences, will be beneficial.

(c) *A standard requiring specific identification of unallowable costs will only lead to added controversy and impair the freedom of contracting parties to negotiate equitable treatment of costs.*

This issue is closely related to the first issue discussed above, but is addressed to the problems and interpretative differences involved in the classification of costs as allowable or unallowable.

The Board acknowledges that there may seldom be full agreement between the parties to a contract as to all of the specific items of costs which are unallowable under pertinent laws, regulations and contractual provisions, and that negotiation must, therefore, be resorted to as a practical means of resolving differences. The Standard does not contemplate interference with such negotiations. However, by requiring consistent cost accounting recognition and appropriate accounting treatment of costs agreed to be unallowable, or which are authoritatively designated as unallowable, the Standard should encourage more definitive negotiated agreements. More specificity in agreements should help to limit the areas of future negotiation or dispute to those where there is a rational basis for disagreement.

2. *Directly Associated Costs.* The published version of the proposed Standard defined a directly associated cost as, "Any cost which is generated solely as a result of the incurrence of another cost and which would not have been incurred had the other cost not been incurred." It then provided, in effect, that directly associated costs of identified unallowable costs should be included with the unallowable costs with which they are associated, and be accorded similar cost accounting treatment. These provision of the Standard, which were intended solely to cover costs which were incremental with respect to identified unallowable costs, drew comment from disparate sources. Those who disagreed with any attribution of nonallowability to costs which were not unallowable by nature but merely by association were opposed to the directly associated cost concept. Also, some of those favoring such attribution, while not opposed to the concept, interpreted the Standard as encroaching upon, or narrowing the application of, existing regulatory provisions governing cost disallowances, and expressed disagreement with the proposed coverage on this basis. After careful consideration of the comments on this issue, the Board has concluded that coverage in the Standard of directly associated costs is appropriate and necessary.

The Board notes that various regulatory provisions use such nondefinitive terms as "corollary administrative costs," "related collection costs," "related legal costs," "incidental costs relating thereto," "other related costs," etc., in describing unallowable costs. In such cases, the Board considers that the identification and measurement of costs covered by these broadly worded provisions is a function of cost accounting, and therefore appropriate for coverage in this Cost Accounting Standard as directly associated costs.

In light of the above considerations, the Board has retained coverage of directly associated costs. The Board, however, recognizes that treatment of a cost as an unallowable directly associated cost in certain circumstances could result in double counting with respect to a class or category of costs included in an indirect-cost pool that will be allocated over a base containing the designated unallowable costs with which the cost in question is associated. In such circumstances, the Standard requires that the cost shall not be classified as a directly associated cost, but rather shall be retained in the indirect-cost pool and allocated through the regular allocation process.

3. *Expressly Unallowable Costs.* The requirement in the proposed Standard

for contractor identification of "costs which are patently unallowable" gave rise to expressions of concern on the part of number of respondents. These ranged from allegations of general impracticability of compliance to apprehensions that the lack of a clear definition would lead to overzealous implementation by auditors and contracting officers and to increased controversy.

Various alternative suggestions were made by commentators. One such suggestion was that identification be required only when there is mutual agreement on unallowable costs by the parties to a contract. This, however, would be likely to minimize one of the benefits of the Standard; namely, the reduction of the time and effort spent in audit and negotiation covering costs whose nonallowability is obvious. Also, items requiring agreement are covered by other provisions of the Standard.

A second suggestion made by respondents was that this requirement be made applicable only to costs which the contractor considers or determines to be "patently" unallowable. This suggestion, however, is subject to the obvious criticism that any requirement that would provide the party subject thereto with absolute freedom of choice as to what constitutes compliance would be of dubious effectiveness. The Standard, of course, clearly provides for the contractor to be the party having the primary responsibility of making the initial determination as to what costs incurred by him are obviously unallowable.

A third suggestion offered by respondents was that the Standard provide a definition, or examples, covering the costs which are considered to be "patently" unallowable. The Board felt that this suggestion had merit. Because of apparent confusion as to the useage of the term "patently," the Board has substituted the word "expressly" in the Standard, and has included a definition of "expressly unallowable cost." Most of the items of cost that are of the type required to be accounted for as expressly unallowable are specified in agency procurement regulations (e.g., ASPR 15-205). It would not be practical to list the items of cost that may be made expressly unallowable under the specific provisions of contracts. The Board, in its definition of an "expressly unallowable cost," has used the word "expressly" in the broad dictionary sense—that which is in direct or unmistakable terms.

With regard to the stated concern about overzealous implementation by auditors and contracting officers, the Board has previously stated that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable. The Board anticipates that this rule of reason will be applied in the implementation of this Standard. Thus, where a good faith effort has been made by a contractor, in the development and implementation of his cost accounting rules, procedures, and practices, to provide for identification of expressly unallowable costs, it is intended that inadvertent failure to properly classify a particular item of cost will not be regarded as noncompliance.

The Board has retained the requirement for contractor identification of costs which are unequivocally made unallowable by the express provisions of an applicable law, regulation or contract. The Standard, however, has been revised to make clearer the accounting distinction between costs which are either expressly unallowable or mutually agreed to be unallowable and costs which are designated as unallowable by the unilateral exercise of a contracting officer's authority under contract disputes procedures. Solely for the purposes of this distinction, the provision in the revised Standard setting forth the identification requirement for expressly unallowable and mutually-agreed unallowable costs also specifies that these are costs which shall be excluded from Government-contract billings, claims, or proposals.

4. *Indirect-cost allocation bases.* By far the largest number of comments were addressed to the requirement in paragraph (c) of § 405.40 of the proposed Standard, that unallowable costs shall be subject to the same cost accounting requirements as allowable costs in determining the content of cost-oriented bases for allocation of indirect costs. This is an issue which appears to have produced an almost com-

plete polarization of the viewpoints of Government representatives and of the parties with whom they contract.

Current agency regulations (e.g. ASPR 15-203(c)) provide, in essence, that indirect-cost allocation bases should not be fragmented for purposes of removing individual elements therefrom. They therefore provide that unallowable costs in an allocation base shall "bear" their pro rata share of the indirect costs in the pool being distributed. The wording of these regulatory provisions has commonly been interpreted as meaning that the indirect costs shall assume the allowability status of the costs in the allocation base. Comments on this regulatory requirement, therefore, have centered on the issue of making otherwise allowable costs unallowable, rather than on the broader accounting principles that should govern cost allocation.

As previously indicated, the Board believes that the issues concerning cost allocation and those relating to cost allowance are distinct and separate. Allowability should not be a factor in the selection or in the determination of the content of an allocation base used to distribute a pool of indirect costs. The appropriateness of a particular allocation base should be determined primarily in terms of its distributive characteristics. Any selective fragmentation of that base which eliminates given base elements for only some of the relevant cost objectives would produce a distortion in the resulting allocations. The Board, therefore, is retaining the requirement that unallowable costs be subject to the same cost accounting principles as those governing allowable costs.

When an item, activity, or function has been deemed unallowable by other relevant authority, the Board in this Standard has approached the determination of the costs related to the unallowable item, activity, or function in three stages: (a) Its direct cost, (b) its directly associated cost, and (c) the indirect costs allocable by means of a base containing such costs. This has been done because, while there is usually no question that the relevant authority intended that the direct cost (a) be disallowed, there may be questions as to whether costs (b) and (c), otherwise allowable, were intended to be disallowed. The latter two costs are, therefore, required to be separately identified and measured so that their allowability can be resolved through the procurement process.

In concluding that indirect-cost allocation bases should not be fragmented solely for purposes of removing unallowable base elements, the Board is not implying that the elimination of all or part of a base element for other purposes is always inappropriate and inconsistent with sound cost accounting.

5. *Contracting Officer decision.* Many respondents questioned the requirement, in § 405.40(a) of the proposed Standard, for identifying as unallowable those costs "designated as unallowable as a result * * * of * * * a final decision of the contracting officer issued pursuant to contract disputes procedures." Concern was expressed that this gave too much standing to the unilateral administrative decision of the contracting officer, and did not recognize contractors' right of appeal to the boards of contract appeals and the courts.

The Board recognizes that legitimate disagreements over allowability often are not finally resolved by contracting officers' decisions. The Board notes, however, that the Standard distinguishes between costs which are "expressly unallowable" and costs which are "designated as unallowable." To further the distinction, and to remove a possible source of misinterpretation, the words "final decision" have been changed to "written decision," to conform to wording in agency regulations governing disputes procedures. The Board believes that, although the written decisions of contracting officers pursuant to formal disputes clause procedures are subject to appeal and possible reversal, they nevertheless constitute authoritative designations, and represent the culmination of a process of audit and negotiation. Furthermore, they are binding on the parties to a contract until and unless changed on appeal. The Board, therefore, considers that any definitive designations of unallowable costs which are provided in the contracting officers' written decisions warrant identification, and it has retained this requirement.

A further objection was raised by some commentators to the requirement, in paragraph (a) of § 405.50 of the published proposal, for future recognition of costs identified as unallowable, or of other costs incurred for the same purpose in like circumstances. The observation was made that future circumstances might warrant different conclusions as to allowability.

The Board recognizes that identical costs may be unallowable under one set of circumstances, but nevertheless be determined to be allowable under different conditions, or as a result of changed criteria. The Board, however, believes that specific designations of the allowability status of particular classes or categories of cost should be given consideration in the evaluations of any like costs which are governed by the same allowability criteria and which are incurred for the same purpose in like circumstances. The provisions in the Standard which reflect this viewpoint have been clarified.

The Board notes that the identification of costs covered by an adverse contracting officer decision will not prevent a contractor from continuing to claim such costs, where disagreement as to allowability continues. It serves merely to identify the costs for special consideration, thereby helping to assure adequate reevaluations, and to promote resolution of the issues involved in the disagreement. Reversal of the contracting officer's decision by a final appeals board or court ruling would, of course, relieve the contractor of any identification requirement under the Standard covering the costs involved in the ruling.

6. *Accountability for unallowable costs.* A number of comments were received concerning what some writers interpreted as an unnecessary and improper requirement for detailed accountability covering costs which are absorbed by the contractor and therefore should not be of any legitimate concern to the customer. The Board does not intend requiring cost identification or cost allocation which is not relevant to the determination of Government contract cost. The Standard requires identification of unallowable costs only to the extent needed for audit verification of the costs which are included in, or which provide backup support for, proposals, billings, or claims. Appropriate revisions have been made in the Standard.

7. *Colleges and universities.* A number of comments were received from university officials expressing concern that, because colleges and universities contracting with the Government are subject to a different set of contract cost reimbursement principles than commercial organizations, and operate in a different accounting environment, the proposed Standard might present implementation problems if applied to these institutions. These comments have been carefully considered, and supplementary discussions have been held with some of the officials concerned.

On the basis of its analysis of the practices described by commentators as having been deemed acceptable in the past, and of the underlying principles and contractual requirements, the Board believes that the Standard, as revised, can be applied to colleges and universities without any disruption of practices which are acceptable under applicable laws and regulations.

Particular concern was expressed over what was reported to be a common situation, where certain costs, such as faculty salaries, are excluded from contract costs even though such costs may directly pertain to work performance which is an intrinsic part of the contract project. The Board notes that specific identification with, or allocation to, individual contracts and other final cost objectives is not required for costs which will not be included in, nor constitute pertinent backup support for, any proposal, billing, or claim. The Standard requires only that sufficient identification be provided to enable verification of the allocability status of unallowable costs and the accounting treatment actually accorded such costs. The Board, therefore, does not believe that any special provision is required covering the situation described.

8. *Materiality.* A number of comments were received suggesting that the question of materiality be given more consideration in the Standard.

The recognition of the materiality problem in paragraph (f) of § 405.50 of the proposed standard was endorsed, but concern was expressed that limiting application to circumstances where there was a "low incidence of negotiated Government contracts relative to other types of work" would render the provision ineffective.

Several instances of potential problem areas were mentioned. One of these concerned the situation where corporate headquarters' expenses are allocated to segments which are involved in a relatively insignificant volume of Government contract work. Another cited the case of a standard cost accounting system covering the manufacture of standard products which may incidentally be used as material or components in contract work. A third referred to the problem of determining "true" cost of an individual product in a joint-product, joint-cost production situation. Another problem area is that involving determination of the share of indirect expense to be assigned as costs of a proscribed organizational or functional activity.

The Board recognizes that accounting for unallowable costs (which are themselves often determined only through negotiation) is an area where the question of materiality should be given special consideration. In providing this consideration, many factors should be taken into account. These include not only the materiality of the total unallowable costs, but also the materiality of the refinements in determinations of unallowable costs which might be achieved through requiring detailed application of the Standard, as contrasted with negotiating the agreements authorized under the proposed paragraph (f) of § 405.50. The Board, accordingly, has revised the Standard to include an amended paragraph (c) which, "based upon considerations of materiality," permits agreements that will satisfy the purpose of the Standard. The Board believes that, in applying the materiality provision of the revised paragraph (c), consideration should be given to the criteria listed in the section titled "MATERIALITY" in the Board's March 1973 "Statement of Operating Policies, Procedures and Objectives."

9. *Improperly allocated costs.* One commentator raised a question concerning the accounting treatment to be accorded costs which are disallowed because they are erroneously allocated to the contract under which they are claimed. The Board does not believe that the Standard needs to deal with accounting errors of this type. It is obvious that the accounting treatment to be accorded any item of cost should be determined by that cost's correct positioning in the cost accounting structure.

10. *Cost/benefit.* Only limited comments were received on the subject of the implementation cost of the Standard, and several of these indicated only minimal impact. Of those claiming significant additional implementation expense, none provided any data as justification for the claim. The Board has concluded from its research that the Standard, as revised, constitutes a reasonable requirement, and that the costs of implementation will be minimal. The potential benefits to the audit and negotiation processes accruing from the increase in visibility and in uniformity of cost accounting treatment will be substantial and will greatly outweigh any added costs.

11. *Effective date and application.* With respect to the date that this standard becomes effective, it is anticipated that its provisions will be applicable to all solicitations issued on or after January 1, 1974, which are likely to lead to contracts covered by Standards, rules, and regulations of the Cost Accounting Standards Board.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part the words and phrases defined in § 405.30 of the Standard.

PREAMBLE B

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 405.10. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 405.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

* * * * *

In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 406—COST ACCOUNTING STANDARD—COST ACCOUNTING PERIOD

Sec.
406.10 General applicability.
406.20 Purpose.
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406.80 Effective date.
PREAMBLES A—B

AUTHORITY: Sec. 719, Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. app. 2168).

SOURCE: 38 FR 30732, Nov. 7, 1973 unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (38 FR 30732, November 7, 1973) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 406.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

PREAMBLES: For preamble to § 406.10, see preamble B of the supplement to this part. For preamble to superseded regulations see preamble A of the supplement.

§ 406.20 Purpose.

The purpose of this Cost Accounting Standard is to provide criteria for the selection of the time periods to be used as cost accounting periods for contract cost estimating, accumulating, and reporting. This Standard will reduce the effects of variations in the flow of costs within each cost accounting period. It will also enhance objectivity, consistency, and verifiability, and promote uniformity and comparability in contract cost measurements.

§ 406.30 Definitions.

(a) The following definitions which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Allocate.* To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Cost objective.* A function, organizational subdivision, contract or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

(3) *Fiscal year.* The accounting period for which annual financial statements are regularly prepared, generally a period of 12 months, 52 weeks, or 53 weeks.

(4) *Indirect cost pool.* A grouping of incurred costs identified with two or more cost objectives but not identified specifically with any final cost objective.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable: None.

§ 406.40 Fundamental requirement.

(a) A contractor shall use this fiscal year as his cost accounting period, except that:

(1) Costs of an indirect function which exists for only a part of a cost accounting period may be allocated to cost objectives of that same part of the period as provided in § 406.50(a).

(2) An annual period other than the fiscal year may, as provided in § 406.50μ(d), be used as the cost accounting period if its use is an established practice of the contractor.

(3) A transitional cost accounting period other than a year shall be used whenever a change of fiscal year occurs.

(4) Where a contractor's cost accounting period is different from the reporting period required by Renegotiation Board regulations, the latter may be used for such reporting.

(b) A contractor shall follow consistent practices in his selection of the cost accounting period or periods in which any types of expense and any types of adjustment to expense (including prior-period adjustments) are accumulated and allocated.

(c) The same cost accounting period shall be used for accumulating costs in an indirect cost pool as for establishing its allocation base, except that the contracting parties may agree to use a different period for establishing an allocation base as provided in § 406.50(e).

§ 406.50 Techniques for application.

(a) The cost of an indirect function which exists for only a part of a cost accounting period may be allocated on the basis of data for that part of the cost accounting period if the cost is (1) material in amount, (2) accumulated in a separate indirect cost pool, and (3) allocated on the basis of an appropriate direct measure of the activity or output of the function during that part of the period.

(b) The practices required by § 406.40(b) of this Standard shall include appropriate practices for deferrals, accruals, and other adjustments to be used in identifying the cost accounting periods among which any types of expense and any types of adjustment to expense are distributed. If an expense, such as taxes, insurance or employee leave, is identified with a fixed, recurring, annual period which is different from the contractor's cost accounting period, the Standard permits continued use of that different period. Such expenses shall be distributed to cost accounting periods in accordance with the contractor's established practices for accruals, deferrals and other adjustments.

(c) Indirect cost allocation rates, based on estimates, which are used for the purpose of expediting the closing of contracts which are terminated or completed prior to the end of a cost accounting period need not be those finally determined or negotiated for that cost accounting period. They shall, however, be developed to represent a full cost accounting period, except as provided in paragraph (a) of this section.

(d) A contractor may, upon mutual agreement with the Government, use as his cost accounting period a fixed annual period other than his fiscal year, if the use of such a period is an established practice of the contractor and is consistently used for managing and controlling the business, and appropriate accruals, deferrals or other adjustments are made with respect to such annual periods.

(e) The contracting parties may agree to use an annual period which does not coincide precisely with the cost accounting period for developing the data used in establishing an allocation base: *Provided,*

(1) The practice is necessary to obtain significant administrative convenience, (2) the practice is consistently followed by the contractor, (3) the annual period used is representative of the activity of the cost accounting period for which the indirect costs to be allocated are accumulated, and (4) the practice can reasonably be estimated to provide a distribution to cost objective of the cost accounting period not materially different from that which otherwise would be obtained.

(f) When a transitional cost accounting period is required under the provisions of § 406.40(a)(3), the contractor may select any one of the following:

(1) The period, less than a year in length, extending from the end of his previous cost accounting period to the beginning of his next regular cost accounting period; (2) a period in excess of a year, but not longer than fifteen months, obtained by combining the period described in paragraph (f)(1) of this section with the previous cost accounting period; or (3) a period in excess of a year, but not longer than fifteen months, obtained by combining the period described in paragraph (f)(1) of this section with the next regular cost accounting period. A change in the contractor's cost accounting period is a change in accounting practices for which an adjustment in the contract price may be required in accordance with paragraph (a)(4)(B) or (C) of the contract clause set out at § 331.50 of this chapter.

[38 FR 30732, Nov. 7, 1973, as amended at 43 FR 9781, Mar. 10, 1978]

PREAMBLE

For preamble relating to § 406.50(f), see preamble J of the supplement to Part 331.

§ 406.60 Illustrations.

(a) A contractor allocates general management expenses on the basis of total cost input. In a proposal for a covered negotiated fixed-price contract, he estimates the allocable expenses based solely on the estimated amount of the general management expense pool and the amount of the total cost input base estimated to be incurred during the eight months in which performance is scheduled to be commenced and completed. Such a proposal would be in violation of the requirements of this Standard that the calculation of the amounts of both the indirect cost pools and the allocation bases be based on the contractor's cost accounting period.

(b) A contractor whose cost accounting period is the calendar year, installs a computer service center to begin operations on May 1. The operating expense related to the new service center is expeected to be material in amount, will be accumulated in a separate indirect cost pool, and will be allocated to the benefiting cost objectives on the basis of measured usage. The total operating expenses of the computer service center for the eight-month part of the cost accounting period may be allocated to the benefiting cost objectives of that same eight-month period.

(c) A contractor changes his fiscal year from a calendar year to the 12-month period ending May 31. For financial reporting purposes, he has a five-month transitional "fiscal year." The same five-month period must be used as the transitional cost accounting period; it may not be combined as provided in § 406.50(f), because the transitional period would be longer than fifteen months. The new fiscal year must be adopted thereafter as his regular cost accounting period. The change in his cost accounting period is a change in accounting practices; adjustments of the contract prices may thereafter be required in accordance with paragraph (a)(4)(B) or (C) of the contract clause set out at § 331.50 of this chapter.

(d) Financial reports to stockholders are made on a calendar year basis for the entire contractor corporation. However, the contracting segment does all internal financial planning, budgeting, and internal reporting on the basis of a "model year." The contracting parties agree to use a "model year" and they agree to overhead rates on the "model year" basis. They also agree on a technique for prorating fiscal year assignment of corporate home office expenses between model years. This practice is permitted by the Standard.

(e) Most financial accounts and contract cost records are maintained on the basis of a fiscal year which ends November 30 each year. However, employee vacation allowances are regularly managed on the basis of a "vacation year" which ends September 30 each year. Vacation expenses are estimated uniformly during each "vacation year." Adjustments are made each October to adjust the accrued liability to actual, and the estimating rates are modified to the extent deemed appropriate. This use of a separate annual period for determining the amounts of vacation expense is permitted under § 406.50(b).

[38 FR 30732, Nov. 7, 1973, as amended at 43 FR 9781, Mar. 10, 1978]

PREAMBLE

For preamble relating to § 406.50(f), see preamble J of the supplement to Part 331.

§ 406.70 Exemptions.

None.

§ 406.80 Effective date.

(a) The effective date of this Standard is July 1, 1974.

(b) This Standard shall be followed by each contractor as of the start of his next fiscal year beginning after receipt of a contract to which this Standard is applicable.

[38 FR 30732, Nov. 7, 1973, as amended at 39 FR 10115, Mar. 18, 1974]

PREAMBLE: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined.

PREAMBLE A

Preamble to Original Publication, 11-7-73

The material below is the preamble to the original publication of Part 406, on Nov. 7, 1973, at 38 FR 30732.

The Standard on Cost Accounting Period published today is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. app. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Standard was initiated as the result of recognition that the selection of time periods to be used for contract cost accumulation and allocation has been the source of continuing problems between contractors and the Government. The problems include:

(1) The lack of a firm requirement specifying the cost accounting period to be used, (2) the absence of specificity as to when a cost accounting period other than a contractor's fiscal year should be used, and (3) the lack of consistency in selecting the cost accounting period in which specific types of expenses and adjustments are recognized.

Early research on this Standard included an extensive review of available literature on the subject and a review of decisions of contract appeals boards and courts. A preliminary draft of the Standard on Cost Accounting Period was widely distributed for informal comment by interested parties.

The Standard now being promulgated is derived from the proposal which was published in the FEDERAL REGISTER for August 7, 1973, with an invitation for interested parties to submit data, views, and arguments to the Board. The Board supplemented that FEDERAL REGISTER publication by sending copies of the FEDERAL REGISTER directly to organizations and individuals who were expected to be interested. Responses were received from 50 sources, including individual companies, Government agencies, professional associations, and industry associations. All of the comments have been carefully considered by the Board.

Most of those who replied to the Board's solicitation indicated satisfaction with the proposal as published. Several contractors indicated that their practices already complied with the Standard. Several commentators voiced objection to parts of the Standard.

The Board takes this opportunity to express its appreciation for the helpful suggestions and constructive criticisms which have been furnished, both informally in response to the circulation of a Staff draft of a Standard and formally in response to the initial FEDERAL REGISTER publication.

The comments below summarize the major issues raised in connection with the August 7 proposal and explain the decisions which have been made.

(1) *Monthly allocations.* A few commentators felt that the Standard should permit monthly allocations of indirect costs on the basis of the data accumulated for each month. This alternative was considered by the Board; however, the idea of monthly cost accounting periods is not appropriate for contract cost accounting. A number of fairly stringent requirements for accruals, deferrals, and other adjustments would have to be incorporated

in the provisions of any Standard if there were to be assurance that monthly accruals, deferrals, and other adjustments were appropriate. The administrative costs would outweigh any benefits. To allow monthly closings for some contract situations and to require full-year allocations for others would not be in the interest of comparability and uniformity. The Board, therefore, has not adopted the suggestion.

(2) *Identity of cost accounting periods for indirect cost pools and allocation bases.* A few commentators stated that it may not be necessary to require in every instance the identical allocation base period as the cost accumulation period. They stated that they presently use various clerical expedients to accomplish this, such as measuring the base for a period other than, but representative of the activity of, the period used for accumulating costs in an indirect cost pool. As a matter of principle, the Board does not agree that mismatched periods are proper. The Board, however, recognizes the value of appropriate expedients where cost allocations are not expected to be materially affected. It acknowledges that there may be occasions when it is necessary to use combinations of actual and estimated data to comply with this Standard.

The Board has given recognition to issues of materiality in its Statement of Operating Policies, Procedures, and Objectives in the FEDERAL REGISTER of March 6, 1973, and believes that materiality should be considered in the administration of its Standards. In order to alleviate practical problems which might be experienced in implementing this concept of materiality, the Board has changed § 406.40(c) and has added § 406.50(e).

(3) *Use of a cost accounting period for estimating.* Several commentators stated that § 406.50(c) was ambiguous. Some pointed out that this provision might be interpreted as always requiring the use of a full fiscal year, not withstanding the permissible use of a short period under the conditions provided in § 406.50(a). There was no provision in § 406.50(a) which precluded its application, when appropriate, in the circumstances described in § 406.50(c). Nevertheless, the Board has modified § 406.50(c) to assure that there is no misinterpretation of its intent.

One commentator recommended that detailed guidelines be established for estimating cost data when estimates were necessary under the provisions of § 406.50(c). The Board believes that this is a matter of contract administration and negotiation. If the parties do not agree on proposed overhead rates for early settlement or closing of contracts, they are not required by this Standard to agree to an expedited settlement.

Two commentators recommended that variances resulting from a difference between the estimated overhead rates used for expediting the closing of contracts and the rates finally negotiated or determined for a cost accounting period should be accounted for by making appropriate eliminations from affected indirect cost pools and allocation bases. As a matter of principle, the Board believes that actual cost should be allocated in accordance with the contractor's disclosed or established practices to all cost objectives of the cost accounting period, including closed or settled contracts. In a settlement the price is fixed, but costs are not. By agreeing to a settlement price, the parties take the risk that actual costs allocated to that contract might be higher or lower than expected. However, the Board finds no need to specify how variances are to be accounted for in this Standard. Normally, the expected variances will be estimated to be minor in amount, or the parties will not agree on the settlement price. Also, the manner of accounting for the actual variance should be agreed upon by the contractor and the Administrative Contracting Officer. If the amount is negligible, it may be agreed that it should be absorbed by other cost objectives of the period. In any event, the Board believes that this is a matter of contract administration and negotiation.

(4) *Terminations.* A few commentators recommended that guidance be provided in § 406.50(c) for the treatment of unabsorbed overhead and continuing overhead charges allocable to contract terminations. The Board has

noted the possible need for Cost Accounting Standards on termination costs and delay claims, situations in which the problems of unabsorbed overhead and continuing overhead charges frequently arise, and has initiated research projects on those subjects. At this time, the Board sees no need to disturb the expectations of the parties to a contract with respect to the absorption of overhead assigned to cost accounting periods (normally, fiscal years) by cost objectives of those same periods, whether or not those cost objectives exist throughout a cost accounting period.

(5) *Applicability of the standard to both direct and indirect costs.* One commentator recommended that the Standard be applied only to indirect costs. The Standard does apply to both direct costs and indirect costs as those terms are defined in 4 CFR Part 400. However, this Standard also includes provisions with specific applicability only to indirect cost pools. The Standard does not require that direct costs be allocated in the same manner as indirect costs. For example, it does not require that direct costs be annualized or averaged for purposes of cost allocation. Direct costs, however, are often used in establishing allocation bases for a period; therefore, they must be assigned and accounted for as costs of the particular cost accounting periods to which they are applicable. Consistency in making adjustments to both direct and indirect costs for purposes of determining the total costs allocable to the cost objectives of a cost accounting period is an important objective of this Standard.

(6) *Permitting the use of periods less than a year.* A few interested parties recommended that the Standard permit the use of a period shorter than a fiscal year when, for example, a significant contract was begun or concluded during a fiscal year. No one advanced any criteria for determining when to use a short period or how to apply it, even after specific requests for such suggestions. The only rationale advanced for using less than an annual period in such circumstances was the assertion that a short period might be employed to arrive at "more equitable allocations," or to avoid inequitable burdens on other cost objectives. In view of the vagueness of the criterion of "equity," the possible effect of changing the risks assumed by the respective parties at the time of contracting, the possible impact on matters of cost allowability and contract administration and negotiation responsibilities, and the continuance of disputes and disagreements over the equity of a short period in particular circumstances, the Board has concluded that the Standard should not authorize the use of a short period except for allocating the costs of an indirect function which exists for only a part of a cost accounting period and for establishing a transitional period when a change of fiscal year occurs. As published this Standard precludes either party to the contract from insisting upon a short period in order to maximize or minimize cost recoupment. It precludes, for example, the calculation of overhead rates after-the-fact for alternative application on the basis of either the fiscal year or the period of performance, and the consequent polarization of the positions of the parties as to which period is appropriate or "equitable" when there is a substantial difference between these rates. The Board believes that this Standard will significantly enhance fairness and objectivity in this regard.

(7) *Equitable adjustments.* One professional accounting organization requested that a specific provision be added whereby an equitable adjustment would be made where the contract cost was affected by a change in the contractor's fiscal year and the change in the fiscal year was adopted for financial accounting and income tax purposes as well as for contract cost accounting. The principal argument advanced for this position is that "there seems to be no valid reason why a contractor should necessarily suffer and the Government should necessarily benefit in such a circumstance." In the illustration in § 406.60(c), the Board noted that under this Standard, a change in the fiscal year data is a change in accounting practices, and that an adjustment of the contract price might therefore be required in accordance with the ad-

justment provisions of the contract clause set out at 4 CFR 331.50. Those provisions do contemplate that no change in disclosed or established cost accounting practices, other than changes under paragraph (a)(4)(A) of the clause, may result in an agreement whereby costs paid by the United States are increased. The Board recognizes that a contractor may change his fiscal year ending date for substantial business reasons, and has illustrated this possibility in the Standard. A change in fiscal year may not have any cost impact. Where it does, the Board believes that it would be improper for the Government to agree to pay increased costs caused by a voluntary change in accounting practices, no matter how valid and unrelated to cost recovery the motives of the contractor for making the change in this fiscal year ending date may have been. A new paragraph (f) in § 406.50 makes it clear that a change in the contractor's cost accounting period is a change in accounting practices for which an adjustment in contract prices may be required in accordance with paragraph (a)(4)(B) of the contract clause set out at 4 CFR 331.50.

(8) *Choice of transitional period.* A public accounting firm suggested that it might help to avoid disagreements if the Standard made it clear as to the permissible choices in selecting the transitional period other than a year whenever a change of fiscal year occurred. This suggestion has been adopted in the new paragraph (f) of § 406.50.

(9) *Applicability to Renegotiation Board.* One commentator noted that the Renegotiation Board, a "relevant Federal agency" under Pub. L. 91-379, defines the term "fiscal year" to mean the taxable year of the contractor or subcontractor under Chapter I of the Internal Revenue Code, and that it has been the Renegotiation Board's practice to renegotiate a contractor on the same basis as the contractor reports for Federal income tax purposes. Hence, it was recommended that, especially because of §§ 406.40(a)(2) and 406.50(d) of the Standard, the Renegotiation Board be exempted from the application of the Standard.

The Board's research confirms the possibility that a few contractors may use cost accounting periods which are different from their tax years. In most cases, however, there will be no conflict. Where there are differences, any use of a cost accounting period or fiscal year which is not identical with the period used for Federal income tax reports will involve reconciliations by the taxpayer. Contractors who presently use "model years" for their cost accounting periods now file reports with the Renegotiation Board on a taxable year basis. The Board finds no need to disturb this practice, and has provided a new § 406.40(a)(4) to acknowledge it as an exception. The Board believes that the Standard is, however, otherwise applicable, and that there is no need for an exemption.

(10) *Comparing benefits and costs.* The Board concludes that this Standard as published herein has, for most contractors and for the Government, almost no cost impact. The only contrary expressions received in response to our requests have been answered by the changes described above. One major Defense agency expressed concern that the Standard might result in higher cost allocations to its contracts insofar as it did not permit the use of short periods. While this may be true, the Standard might also yield lower cost allocations to Government contracts as a result of the requirement to use a full fiscal year. No estimate of the amount of any shifts in cost allocations was provided. Because of the different circumstances of each application of the requirement, both increases and decreases in cost allocations can be expected.

The Board concludes that significant benefits, far outweighing any costs of implementation, will be realized from the promulgation of this Standard. Such benefits include reduction of disagreements and disputes; increased consistency, fairness, and objectivity; and improvement of estimates for proposals.

(11) *Effective date.* It is anticipated that the effective date in § 406.80(a) may be July 1, 1974.

There is also being published in this document an amendment to Part 400, Definitions, to incorporate in that part the term "fiscal year" defined in § 406.30 of the Standard.

PREAMBLE B

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 406.10. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 406.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

* * * * *

In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 407—USE OF STANDARD COSTS FOR DIRECT MATERIAL AND DIRECT LABOR

Sec.
407.10 General applicability.
407.20 Purpose.
407.30 Definitions.
407.40 Fundamental requirement.
407.50 Techniques for application.
407.60 Illustrations.
407.70 Exemptions.
407.80 Effective date.
PREAMBLES A—B

AUTHORITY: 84 Stat. 796, sec. 103, 50 U.S.C. App. 2168.

SOURCE: 39 FR 11871, Apr. 1, 1974, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (39 FR 11871, April 1, 1974) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 407.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

Preambles: For preamble to § 407.10, see preamble B of the supplement to this part. For preamble to superseded regulations see preamble A of the supplement.

§ 407.20 Purpose.

(a) The purpose of this Cost Accounting Standard is to provide criteria under which standard costs may be used for estimating, accumulating, and reporting costs of direct material and direct labor; and to provide criteria relating to the establishment of standards, accumulation of standard costs, and accumulation and disposition of variances from standard costs. Consistent application of these criteria where standard costs are in use will improve cost measurement and cost assignment.

(b) This Cost Accounting Standard is not intended to cover the use of preestablished measures solely for estimating.

§ 407.30 Definitions.

(a) The following definitions of terms which are prominent in this Cost Accounting Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Cost Accounting Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Labor cost at standard.* A pre-established measure of the labor ele-

ment of cost, computed by multiplying labor-rate standard by labor-time standard.

(2) *Labor-rate standard.* A pre-established measure, expressed in monetary terms, of the price of labor.

(3) *Labor-time standard.* A pre-established measure, expressed in temporal terms, of the quantity of labor.

(4) *Material cost at standard.* A pre-established measure of the material element of cost, computed by multiplying material-price standard by material-quantity standard.

(5) *Material-price standard.* A pre-established measure, expressed in monetary terms, of the price of material.

(6) *Material-quantity standard.* A pre-established measure, expressed in physical terms, of the quantity of material.

(7) *Production unit.* A grouping of activities which either uses homogeneous inputs of direct material and direct labor or yields homogeneous outputs such that the costs or statistics related to these homogeneous inputs or outputs are appropriate as bases for allocating variances.

(8) *Standard cost.* Any cost computed with the use of pre-established measures.

(9) *Variance.* The difference between a pre-established measure and an actual measure.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Cost Accounting Standard:

(1) *Actual cost.* An amount determined on the basis of cost incurred.

§ 407.40 Fundamental requirement.

Standard costs may be used for estimating, accumulating, and reporting costs of direct material and direct labor only when all of the following criteria are met:

(a) Standard costs are entered into the books of account;

(b) Standard costs and related variances are appropriately accounted for at the level of the production unit; and

(c) Practices with respect to the setting and revising of standards, use of standard costs, and disposition of variances are stated in writing and are consistently followed.

§ 407.50 Techniques for application.

(a) (1) A contractor's written statement of practices with respect to standards shall include the bases and criteria (such as engineering studies, experience, or other supporting data) used in setting and revising standards; the period during which standards are to remain effective; the level (such as ideal or realistic) at which material-quantity standards and labor-time standards are set; and conditions (such as those expected to prevail at the beginning of a period) which material-price standards and labor-rate standards are designed to reflect.

(2) Where only either the material price or material quantity is set at standard, with the other component stated at actual, the result of the multiplication shall be treated as material cost at standard. Similarly, where only either the labor rate or labor time is set at standard, with the other component stated at actual, the result of the multiplication shall be treated as labor cost at standard.

(3) A labor-rate standard may be set to cover a category of direct labor only if the functions performed within that category are not materially disparate and the employees involved are interchangeable with respect to the functions performed.

(4) A labor-rate standard may be set to cover a group of direct labor workers who perform disparate functions only under either one of the following conditions:

(i) Where that group of workers all work in a single production unit yielding homogeneous outputs (in this case, the same labor-rate standard shall be applied to each worker in that group), or

(ii) Where that group of workers, in the performance of their respective functions, forms an integral team (in this case, a labor-rate standard shall be set for each integral team).

(b) (1) Material-price standards may be used and their related variances may be recognized either at the time purchases of material are entered into the books of account or at the time material cost is allocated to production units.

(2) Where material-price standards are used and related variances are recognized at the time purchases of material are entered into the books of account, they shall be accumulated separately by homogeneous groupings of material. Examples of homogeneous groupings of material are:

(i) Where prices of all items in that grouping of material are expected to fluctuate in the same direction and at substantially the same rate, or

(ii) Where items in that grouping of material are held for use in a single production unit yielding homogeneous outputs.

(3) Where material-price variances are recognized at the time purchases of material are entered into the books of account, variances of each homogeneous grouping of material shall be allocated (except as provided in paragraph (b)(4) of this section), at least annually, to items in purchased-items inventory and to production units receiving items from that homogeneous grouping of material, in accordance with either one of the following practices, which shall be consistently followed:

(i) Items in purchased-items inventory of a homogeneous grouping of material are adjusted from standard cost to actual cost; the balance of the material-price variance, after reflecting these adjustments, shall be allocated to production units on the basis of the total of standard cost of material received from that homogeneous grouping of material by each of the production units; or

(ii) Items, at standard cost, in purchased-items inventory of a homogeneous grouping of material, are treated, collectively, as a production unit; the material-price variance shall be allocated to production units on the basis of standard cost of material received from that homogeneous grouping of material by each of the production units.

(4) Where material-price variances are recognized at the time purchases of material are entered into the books of account, variances of each homogeneous grouping of material which are insignificant may be included in appropriate indirect cost pools for allocation to applicable cost objectives.

(5) Where a material-price variance is allocated to a production unit in accordance with paragraph (b)(3) of this section, it may be combined with material-quantity variance into one material-cost variance for that production unit. A separate material-cost variance shall be accumulated for each production unit.

(6) Where material-price variances are recognized at the time material cost is allocated to production units, these variances and material-quantity variances may be combined into one material-cost variance account.

(c) Labor-cost variances shall be recognized at the time labor cost is introduced into production units. Labor-rate variances and labor-time variances may be combined into one labor-cost variance account. A separate labor-cost variance shall be accumulated for each production unit.

(d) A contractor's established practice with respect to the disposition of variances accumulated by production unit shall be in accordance with one of the following paragraphs:

(1) Variances are allocated to cost objectives (including ending in-process inventory) at least annually. Where a variance related to material is allocated, the allocation shall be on the basis of the material cost at standard, or, where outputs are homogeneous, on the basis of units of output. Similarly, where a variance related to labor is allocated, the allocation shall be on the basis of the labor cost at standard or labor hours at standard, or, where outputs are homogeneous, on the basis of units of output; or

(2) Variances which are immaterial may be included in appropriate indirect cost pools for allocation to applicable cost objectives.

(e) Where variances applicable to covered contracts are allocated by memorandum worksheet adjustments rather than in the books of account, the bases used for adjustment shall be in accordance with those stated in paragraphs (b)(3) and (d) of this section.

§ 407.60 Illustrations.

(a) Contractor A's written practice is to set his material-price standard for an item on the basis of average purchase prices expected to prevail during the calendar year. For that item whose usage from month to month is stable, a purchase contract is generally signed on May 1 of each year for a one-year commitment. The current purchase contract calls for a purchase price of $3 per pound; an increase of 5 percent, or 15¢ per pound, has been announced by the vendor when the new purchase contract comes into effect next May. Contractor A sets his material-price standard for this item at $3.10 per pound for the year ([$3.00×4+$3.15×8]÷12). Since Contractor A sets his material-price standard in accordance with his written practice, he complies with provisions of § 407.40(c) of this Cost Accounting Standard.

(b) Contractor B accumulates, in one account, labor cost at standard for a department in which several categories of direct labor of disparate functions, in different combinations, are used in the manufacture of various dissimilar outputs of the department. Contractor B's department is not a production unit as defined in § 407.30(a)(7) of this Cost Accounting Standard. Modifying his practice so as to comply with the definition of production unit in § 407.30(a)(7), he could accumulate the standard costs and variances separately, (1) for each of the several categories of direct labor, or (2) for each of several sub-departments, with homogeneous output for each of the sub-departments.

(c) Contractor C allocates variances at the end of each month. During the month of March, a production unit has accumulated the following data with respect to labor:

	Labor hours at standard	Labor dollars at standard	Labor cost variance
Balance, March 1	5,000	$25,000	$2,000
Additions in March	15,000	75,000	5,000
Total	20,000	100,000	7,000
Transfers-out in March	8,000	40,000	
Balance, March 31	12,000	60,000	

Using labor hours at standard as the base, Contractor C establishes a labor-cost variance rate of $.35 per standard labor hour ($7,000÷20,000), and deducts $2,800 ($.35×8,000) from the labor-cost variance account, leaving a balance of $4,200 ($7,000—$2,800). Contractor C's practice complies with provisions of § 407.50(d)(1) of this Cost Accounting Standard.

(d) Contractor D, who uses materials the prices of which are expected to fluctuate at different rates, recognizes material-price variances at the time purchases of material are entered into the books of account. He maintains one purchase-price variance account for the whole plant. Purchased items are requisitioned by various production units in the plant. Since prices of material are expected to fluctuate at different rates, this plant-wide grouping does not constitute a homogeneous grouping of material. Contractor D's practice does not comply with provisions of § 407.50(b)(2) of this Cost Accounting Standard. However, if he would maintain several purchased-items inventory accounts, each representing a homogeneous grouping of material, and maintain a material-price variance account for each of these homogeneous groupings of material, Contractor D's practice would comply with § 407.50(b)(2) of this Cost Accounting Standard.

(e) Contractor E recognizes material-price variances at the time purchases of material are entered into the books of account and allocates variances at the end of each month. During the month of May, a homogeneous grouping of material has accumulated the following data:

	Material cost at standard	Material price variance
Inventory, May 1	$150,000	$20,000
Additions in May	1,850,000	120,000
Total	2,000,000	140,000
Requisitions		
Production unit 1	900,000	
Production unit 2	450,000	
Production unit 3	300,000	
Production unit 4	150,000	
Inventory, May 31	200,000	

Contractor E establishes a material-price variance rate of 7% ($140,000÷$2,000,000) and allocates as follows:

	Material cost at standard	Material-price variance rate (percent)	Material-price variance allocation
Production unit 1	$900,000	7	$63,000
Production unit 2	450,000	7	31,500
Production unit 3	300,000	7	21,000
Production unit 4	150,000	7	10,500
Ending inventory of homogeneous grouping of material	200,000	7	14,000
Total	2,000,000		140,000

Contractor E's practice complies with provisions of § 407.50(b)(3)(ii) of this Cost Accounting Standard.

(f) Contractor F makes year-end adjustments for variances attributable to covered contracts. During the year just ended, a covered contract was processed in 4 production units, each with homogeneous outputs. Data with respect to output and to labor of each of the 4 production units are as follows:

Production unit	Total units of output	Total units used by the covered contract	Total labor cost at standard	Total labor-cost variance
1	100,000	10,000	$400,000	$20,000
2	30,000	6,000	900,000	30,000
3	20,000	5,000	600,000	10,000
4	10,000	4,000	500,000	20,000

Since the outputs of each production unit are homogeneous, Contractor F uses the units of output as the basis of making memorandum worksheet adjustments concerning applicable variances, and establishes the following figures:

	Labor-cost variance per unit of output	Units used by the covered contract	Labor-cost variance attributable to the covered contract
Production unit 1	$0.20	10,000	$2,000
Production unit 2	1.00	6,000	6,000
Production unit 3	.50	5,000	2,500
Production unit 4	2.00	4,000	8,000
Total labor-cost variance attributable to the covered contract			18,500

Contractor F makes a year-end adjustment of $18,500 as the labor-cost variances attributable to the covered contract. Contractor F's practice complies with provisions of § 407.50(e) of this Cost Accounting Standard.

§ 407.70 Exemptions.

None for this Cost Accounting Standard.

§ 407.80 Effective date.

(a) The effective date of this Cost Accounting Standard is October 1, 1974.

(b) This Cost Accounting Standard shall be followed by each contractor as of the start of his next fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

[39 FR 11871, Apr. 1, 1974, as amended at 39 FR 28869, Aug. 12, 1974]

PREAMBLE: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined.

PREAMBLE A

Preamble to Original Publication, 4-1-74

Following is the preamble to the original publication of Part 407, on April 1, 1974, at 39 FR 11869.

The Cost Accounting Standard on the Use of Standard Costs for Direct Material and Direct Labor published today is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub L. 91-379, 50 U.S.C. App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Cost Accounting Standard was initiated as the result of the recognition that practices concerning the use of standard costs for contract costing purposes have not been well defined in Government procurement regulations. The Board has undertaken research on this subject with a view that Cost Accounting Standards promulgated on this subject will provide better guidance in the use of standard costs.

Because the subject of standard costs is extremely complex, the Board has elected to address this subject in phases. The Cost Accounting Standard being promulgated covers the use of standard costs for direct material and direct labor; the use of standard costs for service centers and the use of standard costs for overhead represent two other phases of this subject that are currently under research.

Early research on this Cost Accounting Standard included a study of available literature on the subject and of relevant decisions of boards of contract appeals and courts. Following this study, several issues were identified. A review of Disclosure Statements on file suggested that standard costs are in use by a large number of defense contractors. In an effort to learn the reasons underlying the use or non-use of standard costs for contract costing purposes, and to gain a better understanding of the standard-cost practices by companies in different industries, the Board developed and circulated a questionnaire on the use of standard costs. Selected respondents of this questionnaire were then visited for further discussion. Information derived from replies to the questionnaire and from visits suggested the complexity of the subject and the desirability of addressing it in phases. Accordingly, in the preparation of a preliminary draft, the subject was limited to the use of standard costs for direct material and direct labor. This preliminary draft was widely distributed for comment. Incorporating many comments thus received, a revised proposal was drafted and published in the FEDERAL REGISTER of November 21, 1973, with an invitation for interested parties to submit written views and comments to the Board. The Board also supplemented the invitation in the FEDERAL REGISTER by sending copies of that issue directly to several hundred organizations and individuals who had expressed an interest in the proposal or who had provided the Board with comments on the earlier proposal.

These direct and public invitations for comments resulted in the Board's receiving 47 sets of written comments from individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. Some of these commentators also supplemented their written comments with discussions at individual or group meetings. All of these comments and views have been carefully considered by the Board. Those issues that are of significance are discussed below, together with an explanation of the changes made in the Cost Accounting Standard being promulgated from the proposal published in the FEDERAL REGISTER of November 21, 1973.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

1. *Management uses of standard costs.* Several commentators emphasized the value of information generated from the use of standard costs for management-control purposes and urged the Board to retain these control features. The Board agrees with this view and has consequently modified the proposed Standard to better assure that its use will be fully compatible with the use of standard costs for management-control purposes.

2. *Exclusion of overhead and service centers in the Cost Accounting Standard.* A few commentators expressed the view that the Cost Accounting Standard being promulgated should be broadened to include the treatment of overhead and service centers. The Board believes that the Cost Accounting Standard being promulgated may be used effectively without such broadening. Further, because the use of standard costs for overhead and for

service centers involves different issues, the Board believes that this Cost Accounting Standard should be promulgated as is.

3. *Coverage of this standard.* Many commentators suggested that the proposed Standard did not clearly state that the use of standard costs for Government contract costing purposes is at the option of a contractor; they recommended various changes in wording to make this point clear. The Board has accommodated this suggestion by appropriate modifications in § 407.40.

4. *Use of the term production unit.* Many commentators expressed a need for a better understanding of the meaning and significance of the term production unit. As defined in § 407.30(a)(7), a production unit is a grouping of activities which either uses homogeneous inputs of direct material and direct labor or yields homogeneous outputs. Where a grouping of activities meets either one of these two criteria, it is the proper level at which to accumulate standard costs of direct material and direct labor, and to accumulate variances related thereto. Since variances are allocated on the bases of costs and statistics of each production unit, homogeneity of standard costs of direct material and direct labor would assure that data thus accumulated would be appropriate as bases for allocating variances to cost objectives. The concept of homogeneity embodied in the term production unit, then, would permit contractors a degree of flexibility in setting and revising standards based on individual needs and circumstances and still provide for the proper cost assignment of variances.

To further clarify the intended meaning and purpose of a production unit, the Board has added an illustration as § 407.60(b).

5. *Homogeneous grouping of material.* A few commentators suggested that the concept embodied in the term homogeneous grouping of material be enunciated. The Board agrees; accordingly, the Board has added a statement under § 407.50(b)(2) and an illustration as § 407.60(d).

6. *Cost accounting period.* Quite a few commentators felt that relating the establishment of standards to a cost accounting period, which is the subject of a Cost Accounting Standard (4 CFR Part 406), is both undesirable and unnecessary, in view of the differences in industry practices and management needs for establishing and using standards; they urged the Board to reconsider. Upon reconsideration, the Board finds this argument persuasive. The Board has revised § 407.50(a)(1), which provides that a contractor shall state the period during which standards are to remain effective.

7. *Interim revision of standards.* Many commentators stated that, to maintain comparable information for management-evaluation purposes, revising standards during a cost accounting period is undesirable and counterproductive; they suggested the deletion of this provision. The Board finds this suggestion persuasive; accordingly, the Board has deleted this provision from the Cost Accounting Standard being promulgated.

8. *Procedural details.* Several commentators felt that the proposed Cost Accounting Standard contained too much precedural detail. The Board does not share this feeling. This Cost Accounting Standard, in addressing itself to the entire process of standard-cost accounting for direct material and direct labor and to alternatives in each step of the process, necessitates attention to a great many issues. The Board feels that the provisions of this Cost Accounting Standard only reflect the complexity of the subject matter and the diversity of practices being addressed.

9. *Recording allocation of variances in books of account.* A few commentators misconstrued the proposed Cost Accounting Standard and thought that certain provisions required the recording of variance allocations in formal accounting records; they urged the Board to permit the use of adjustments based on memorandum worksheets for covered contracts. To avoid this misconstruction, the Board has made appropriate revisions in the Cost Accounting Standard being promulgated by using the term books of account to mean formal accounting records, and by adding § 407.50(e) to specifical-

ly permit the use of memorandum worksheet adjustments.

10. *Adjustment of material-price variance recognized at the time of purchase.* Several commentators objected to a provision whereby material-price variances, recognized at the time purchases of material are entered into books of account, are allocated between items introduced into production units and items remaining in ending purchased-items inventory. They argued that this provision does not conform to their practices, particularly where the allocation of unfavorable variances would increase inventory carrying values, and that the provision infringes upon financial accounting.

In all its research, the Board gives extensive consideration to existing contractor practices. In this instance, however, the practices advocated by those contractors are likely to create inequities and are without adequate conceptual support. As to the second argument, the Board believes that this provision, which concerns the proper allocation of material-price variances between reporting periods for cost accounting purposes, is compatible with objectives of financial accounting. In view of these considerations, the Board has retained this provision in § 407.50(b)(3).

11. *Annual allocation of variances.* Quite a few commentators felt that a provision that permitted the allocation of variances not more frequently than once each cost accounting period does not reflect industry practices and management needs. The Board finds this argument persuasive. Accordingly, a provision that permits the allocation of variances more frequently than annually has been added under § 407.50(d)(1).

12. *Five percent materiality criterion.* Many commentators to the proposed Cost Accounting Standard objected to the inclusion of a 5 percent materiality criterion as a basis for determining whether variances are allocated to cost objectives or are included in indirect cost pools for subsequent allocation. Several of the commentators felt that the materiality criterion was arbitrary; others felt that it would delay the process of allocation where it is undertaken monthly; and still others felt that it could result in inconsistencies.

The Board's early research showed that a majority of respondents had variances below 5 percent, and quite a few experienced variances below 2 percent. Later, an overwhelming majority of those commenting on a preliminary draft of this Cost Accounting Standard, which contained a 2 percent materiality criterion, suggested that a materiality criterion set at 5 percent would be reasonable.

The intent of the materiality provision was to permit contractors to use a simpler method of allocation of variances where the amount was below the 5 percent level. Nevertheless, the Board is persuaded by the comments received, and has deleted this provision from the Cost Accounting Standard being promulgated. In its stead, the Board, in § 407.50(b)(4) and (d)(2), provides that, where variances are immaterial, such variances may be included in appropriate indirect cost pools for subsequent allocation.

13. *Cost/benefit.* As to benefits, this Standard provides needed criteria which the Board believes will improve cost measurement and will result in more equitable assignment of contract costs. As to costs, the Board anticipates little or no cost of implementation by those contractors who are currently using standard costs: the Standard permits contractors to choose from many recognized standard cost practices. Consequently, the Board believes that the benefits to be derived by this Standard clearly outweigh any costs of implementation.

The Board expects that the effective date of this Cost Accounting Standard will be October 1, 1974.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in § 407.30(a) of this Cost Accounting Standard.

PREAMBLE B

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 407.10. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 407.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

* * * * *

In the Federal Register of February 16, 1977 (42 FR 9391), the Board proposed to amend section 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 408—ACCOUNTING FOR COSTS OF COMPENSATED PERSONAL ABSENCE

Sec.
408.10 General applicability.
408.20 Purpose.
408.30 Definitions.
408.40 Fundamental requirement.
408.50 Techniques for application.
408.60 Illustrations.
408.70 Exemption.
408.80 Effective date.
Preambles A—B

Authority: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

Source: 39 FR 33684, Sept. 19, 1974, unless otherwise noted.

Editorial Note: A supplement, consisting of the preambles to these regulations as they appeared in the Federal Register, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (39 FR 33681, September 19, 1974) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 408.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

Preambles: For preamble to § 408.10, see preamble B of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 408.20 Purpose.

The purpose of this Standard is to improve, and provide uniformity in, the measurement of costs of vacation, sick leave, holiday, and other compensated personal absence for a cost accounting period, and thereby increase the probability that the measured costs are allocated to the proper cost objectives.

§ 408.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meaning ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Compensated personal absence.* Any absence from work for reasons such as illness, vacation, holidays, jury duty or military training, or personal activities, for which an employer pays compensation directly to an employee in accordance with a plan or custom of the employer.

(2) *Entitlement.* An employee's right, whether conditional or unconditional, to receive a determinable amount of compensated personal absence, or pay in lieu thereof.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 408.40 Fundamental requirement.

(a) The costs of compensated personal absence shall be assigned to the cost accounting period or periods in which the entitlement was earned.

(b) The costs of compensated personal absence for an entire cost accounting period shall be allocated pro-rata on an annual basis among the final cost objectives of that period.

§ 408.50 Techniques for application.

(a) *Determinations.* Each plan or custom for compensated personal absence shall be considered separately in determining when entitlement is earned. If a plan or custom is changed or a new plan or custom is adopted, then a new determination shall be made beginning with the first cost accounting period to which such new or changed plan or custom applies.

(b) *Measurement of entitlement.* (1) For purposes of compliance with § 408.40(a), compensated personal absence is earned at the same time and in the same amount as the employer becomes liable to compensate the employee for such absence if the employer terminates the employee's employment for lack of work or other reasons not involving disciplinary action, in accordance with a plan or custom of the employer. Where a new employee must complete a probationary period before the employer becomes liable, the employer may nonetheless treat such service as creating entitlement in any computations required by this Standard, provided that he does so consistently.

(2) Where a plan or custom provides for entitlement to be determined as of the first calendar day or the first business day of a cost accounting period based on service in the preceding cost accounting period, the entitlement shall be considered to have been earned, and the employer's liability to have arisen, as of the close of the preceding cost accounting period.

(3) In the absence of a determinable liability, in accordance with paragraph (b)(1) of this section, compensated personal absence will be considered to be earned only in the cost accounting period in which it is paid.

(c) *Determination of employer's liability.* In computing the cost of compensated personal absence, the computation shall give effect to the employer's liability in accordance with the following paragraphs:

(1) The estimated liability shall include all earned entitlement to compensated personal absence which exists at the time the liability is determined, in accordance with paragraph (b) of this section.

(2) The estimated liability shall be reduced to allow for anticipated nonutilization, if material.

(3) The liability shall be estimated consistently either in terms of current or of anticipated wage rates. Estimates may be made with respect to individual employees, but such individual estimates shall not be required if the total cost with respect to all employees in the plan can be estimated with reasonable accuracy by the use of sample data, experience or other appropriate means.

(d) *Adjustments.* (1) The estimate of the employer's liability for compensated personal absence at the beginning of the first cost accounting period for which a contractor must comply with this Standard shall be based on the contractor's plan or custom applicable to that period, notwithstanding that some part of that liability has not previously been recognized for contract costing purposes. Any excess of the amount of the liability as determined in accordance with paragraph (c) of this section over the corresponding amount of the liability as determined in accordance with the contractor's previous practice shall be held in suspense and accounted for as described in paragraph (3) of this paragraph (d).

(2) If a plan or custom is changed or a new plan or custom is adopted, and the new determination made in accordance with paragraph (a) of this section results in an increase in the estimate of the employer's liability for compensated personal absence at the beginning of the first cost accounting period for which the new plan is effective over the estimate made in accordance with the contractor's prior practice, then the amount of such increase shall be held in suspense and accounted for as described in paragraph (d)(3) of this section.

(3) At the close of each cost accounting period, the amount held in suspense shall be reduced by the excess of the amount held in suspense at the beginning of the cost accounting

period over the employer's liability (as estimated in accordance with paragraph (c) of this section) at the end of that cost accounting period. The cost of compensated personal absence assigned to that cost accounting period shall be increased by the amount of the excess.

(e) *Allocations.* Except where the use of a longer or shorter period is permitted by the provisions of the Cost Accounting Standard on Cost Accounting Period (Part 406 of this chapter), the costs of compensated personal absence shall be allocated to cost objectives on a pro-rata basis which reflects the total of such costs and the total of the allocation base for the entire cost accounting period. However, this provision shall not preclude revisions to an allocation rate during a cost accounting period based on revised estimates of period totals.

§ 408.60 Illustrations.

(a) Company A's vacation plan provides that on the anniversary of each employee's hiring date, that employee shall become eligible to receive a two-week vacation with pay. Vacation entitlement must be used within two years or forfeited. An employee who leaves the company voluntarily will be paid for any remaining unused vacation entitlement which was earned through the emloyee's last aniversary date. An employee who is laid off for lack of work will also be paid a pro-rata vacation allowance for service since the employee's last anniversary date. Company A accrues vacation costs each month based on an estimate of the anniversary years which will be completed in that month. At the end of its cost accounting period, Company A adjusts its estimated liability to agree with its actual liability for completed years of service on an individual employee basis.

(1) In order to comply with § 408.50(c), Company A must increase its estimated liability for vacation pay at all times to include the estimated additional amount which would be payable to employees in the event of layoff. The additional liability may be calculated on an individual employee basis or it may be estimated for the employees as a group by the use of sample or historical data.

(2) The following illustrates one method of estimating Company A's liability at the end of its cost accounting period, December 31, with respect to individual employees, in accordance with § 408.50(c).

John Doe, Anniversary date July 10:	
Unused entitlement resulting from completed service years, 24 hrs. at $5	$120
Full months of service since anniversary, 5:	
Pro-rata entitlement on lay-off=80 hrs x 5/12=33.3 hrs. at 15	167
Total	287
Less estimated allowance for forfeitures, 3½ percent	10
Net liability	277

(b) Company B has a vacation plan similar to Company A's, but Company B does not pay pro-rata vacation pay on lay-off for service since the last anniversary date. Company B must include in its estimate of its liability at the end of its cost accounting period only that unused vacation entitlement which results from completed years of service, with allowance for forfeitures if material.

(c) Company C's sick leave plan provides that an employee will accumulate one-half day of sick leave entitlement for each full month of service. Sick leave entitlement may be accumulated without limit, but an employee is paid for sick leave only during actual illness; the Company does not pay for unused sick leave on lay-off. Despite the fact that Company C might be able to estimate the amount which will be paid for sick leave in a future cost accounting period with a high degree of accuracy, it has no liability for payment for unused sick leave entitlement in the event of lay-off. Therefore, in accordance with § 408.50 (b)(3), it must assign to each cost accounting period only the costs of sick leave which it pays in that period.

(d) Company D's vacation plan provides that on July 1, each employee who has been employed by the Company for at least one year shall be entitled to two weeks of vacation. All vacation must be taken between July 1 and September 30. An employee who terminates after September 30 and before July 1 receives no vacation pay. Company D has a cost accounting period which ends on December 31; however, Company D customarily accrues its anticipated liability for vacation pay at July 1 in 12 equal installments over the "vacation year" starting on July 1 of the previous year and ending on June 30 of the current year. Company D has no liability for vacation pay at January 1 or at December 31. In accordance with § 408.50(b)(3), the amount of vacation cost which Company D must assign to each cost accounting period is the amount of such costs paid in that period. Therefore, Company D may not use the "vacation year" ending June 30 to apportion these costs between cost accounting periods.

(e) Company E's cost accounting period ends on December 31. Its vacation plan provides that on January 1, each employee who has been employed for at least one year shall become entitled to two weeks of vacation. The Company does not recognize a liability for vacation pay at December 31 because an employee must be employed on January 1 to be eligible.

(1) Despite the requirement that the employee also be employed on January 1, the necessary service was completed in the preceding cost accounting period. If the other terms of the plan are such that in accordance with this Standard, Company E must recognize its vacation costs on the accrual basis, then in accordance with § 408.50(b)(2), Company E must estimate its vacation costs as if the liability arose on December 31 rather than on the following January 1.

(2) Assume that Company E must comply with this Standard beginning on January 1, 1976. Assume that the employees of Company E earned $90,000 in vacation pay in 1975, all of which will be taken in 1976. Assume, further, that because of reduced employment levels, the employees of Company E will earn only $80,000 in vacation pay in 1976, $5,000 of which will be paid in 1976 because of layoffs. The following example illustrates the computation of vacation pay costs for Company E in 1976:

1976 beginning liability	
With Standard (§ 408.50(d)(1))	$90,000
Without Standard	0
Amount to be held in suspense (§ 408.50(d)(1))	90,000
1976 ending liability	75,000
Plus: Paid in 1976	95,000
Subtotal	170,000
Less: 1976 beginning liability	90,000
1976 vacation cost, basic amount	80,000
Amount in suspense at beginning of 1976	90,000
Less: 1976 ending liability	75,000
Suspense to be written off in 1976, additional 1976 vacation cost (§ 408.50(d)(3))	15,000
1976 basic vacation cost	80,000
Plus: 1976 reduction of suspense	15,000
1976 total vacation cost	95,000

(3) Assume, further, that all of the vacation entitlement which remained at December 31, 1976 ($75,000) is taken in 1977. Also, Company E hires a substantial number of additional employees in 1977, so that the amount of vacation entitlement earned in 1977 is $85,000. The following example illustrates the computation of vacation pay costs for Company E in 1977:

1977 ending liability	$85,000
Plus: Paid in 1977	75,000
Subtotal	160,000
Less: 1977 beginning liability	75,000
1977 vacation cost, basic amount	85,000
Amount in suspense at beginning of 1977[1]	75,000
1977 ending liability[1]	85,000
1977 basic vacation cost	85,000
Plus: 1977 reduction of suspense[1]	0
1977 total vacation cost	85,000

[1] Because the 1977 ending liability exceeds the amount in suspense at the beginning of 1977, there is no reduction of suspense in 1977.

(4) Assume further, that Company E goes out of business in 1978. All employees are terminated and paid both for the $85,000 vacation liability at the end of 1977 and an additional $40,000 earned in 1978. The following example illustrates the computation of vacation pay costs for Company E in 1978:

1978 ending liability	0
Plus: Paid in 1978	$125,000
Subtotal	125,000
Less: 1978 beginning liability	85,000
1978 vacation cost, basic amount	40,000
Amount in suspense at beginning of 1978	75,000
Less: 1978 ending liability	0
Suspense to be written off in 1978; additional 1978 vacation cost (§ 408.50(d)(3))	75,000
1978 basic vacation cost	40,000
Plus: 1978 reduction in suspense	75,000
1978 total vacation cost	115,000

(f) All of the salary costs of Company F's salaried employees are charged to service, administrative, or overhead functions. No accounting entries are made to segregate costs of compensated personal absence of these employees from their other salary costs, although other records are maintained to control the total amount of such absences.

(1) This policy does not violate the requirement of § 408.40(b) if such salaries are charged to overhead or indirect cost pools for subsequent allocation to final cost objectives over annually determined allocation bases which are appropriate for those pools.

(2) If the same policy were followed in the case of engineers whose salaries were directly allocated to two or more final cost objectives, or to both intermediate and final cost objectives, so that costs of compensated personal absence were charged directly to the jobs on which the individuals were working when paid, then this would violate the requirement of § 408.40(b) that these costs be allocated among cost objectives on the basis of the costs of the entire cost accounting period. Only if all salaries were directly allocated to a single final cost objective, as might be the case with personnel assigned to an overseas base for the performance of a single contract, would this practice be in accord with that requirement.

(g) Company G determines a "charging rate" for each employee. The charging rate includes an allowance for compensated personal absence based on average experience. As the employee performs services, the related cost objectives are charged for the services at the charging rate, the employee is paid at his base rate, and the excess is credited to the accrued liability for each benefit. As benefits are paid, the costs are charged against the accrued liabilities. The amount of each accrued liability is adjusted at the end of the costs accounting period, and any difference is adjusted through appropriate overhead accounts in accordance with company policy.

(1) This method is not a violation of § 408.40(b) if it results in allocating the estimated annual costs of compensated personal absence at a rate which reflects the anticipated costs of the entire cost accounting period.

(2) The computation itself must comply with the criteria of § 408.40(a). For example, if the terms of the Company's sick leave plan are such that in accordance with this Standard, the costs should be recognized in the cost accounting period when they are paid, then the computation should be intended to amortize the expected costs of sick leave over the activity of that cost accounting period, leaving no accrued liability for sick leave at the end of the cost accounting period.

§ 408.70 Exemption.

This standard shall not apply to contractors who are subject to the provisions of Federal Management Circular 74-4 (Principles for Determining Costs Applicable to Grants and Contracts with State and Local Governments).

[43 FR 24820, June 8, 1978]

Preambles: For preamble to § 408.70, see preamble B of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement to this part.

§ 408.80 Effective date.

(a) The effective date of this Standard is July 1, 1975.

(b) This Cost Accounting Standard shall be followed by each contractor as of the start of his next fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

[39 FR 33684, Sept. 19, 1974, as amended at 40 FR 14737, Apr. 2, 1975; 40 FR 15865, Apr. 8, 1975]

PREAMBLE: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined.

PREAMBLE A

Preamble to Original Publication, 9-19-74

The following is the preamble to the original publication of Part 408, on Sept. 19, 1974, at 39 FR 33681.

The Cost Accounting Standard on Accounting for Costs of Compensated Personal Absence is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub. L. 91-379, 50 U.S.C. App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. This Standard deals primarily with the amount and time of recognition of costs of compensated personal absence.

Work preliminary to the development of this Cost Accounting Standard was initiated as a part of the study of the larger subject of accounting for labor costs. The costs of compensated personal absence are an important element of labor costs, but under existing procurement regulations there is no assurance that the costs of compensated personal absence are assigned to the cost accounting period in which the related labor is performed and in which the related wage or salary costs are recognized. Because the volume and mix of contracts of a particular contractor may vary significantly from period to period, the assignment of costs to the proper cost accounting periods is important.

Early research on this Cost Accounting Standard included a study of available literature and relevant decisions of boards of contract appeals and courts. Initial meetings were held with major procurement agencies and with a number of contractors, and certain issues were tentatively identified. The relationship of Government procurement regulations to Federal Income Tax laws which govern the accounting for costs of compensated personal absence was explored. It was noted that the exact nature of the employer's liability to employees under a specific plan was an important consideration in determining the income tax treatment which might be permitted. A review of Disclosure Statements on file indicated a disparity in existing accounting practices.

A questionnaire and a statement of issues were then sent to 117 companies, 40 Government agencies, and 53 others, including industry and professional associations, to obtain detailed information, particularly in regard to benefit plans and the reasons for selecting a specific accounting method. Data on benefit plans and accounting practices were received from 68 companies and comments on the issues were received from 37 respondents. Analysis of the data and comments indicated that the issues could be classified broadly into two groups—those relating to the amount and timing of recognition of costs of compensated personal absence and those relating to methods of allocation of these costs to cost objectives. Some problems were noted in connection with the charging of costs of compensated personal absence directly to final cost objectives at the time of payment; these have been addressed in the Standard. Detailed criteria for the allocation of costs of compensated personal absence are not included in this Standard. Additional study of other labor-related costs is being undertaken and when it has been completed such criteria may be provided.

Based on analysis of the responses to the questionnaire and issues paper and on further discussions, a preliminary draft Standard was developed and widely distributed for comment. Comments and suggestions were received from 87 respondents; these comments were considered in developing a revised Standard which was published in the FEDERAL REGISTER of March 4, 1974, with an invitation to interested parties to submit written views and comments to the Board. The Board also supplemented the invitation in the FEDERAL REGISTER by sending copies of that issue to several hundred organizations and individuals who had provided the Board with comments on the earlier proposal or who had otherwise expressed interest in the proposal.

Following the FEDERAL REGISTER publication, the Board received 86 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. All comments have been carefully considered by the Board and those addressing areas of significance are discussed below, together with explanations of the changes made in the Cost Accounting Standard being promulgated from the proposal published in the FEDERAL REGISTER of March 4, 1974.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(1) *Need for a standard.* The most significant problems and issues relate to the amount and timing of recognition of costs of compensated personal absence appear to stem from the reliance of existing procurement regulations on the Internal Revenue Code and income tax regulations to govern accounting for these costs. Three disadvantages arise from this reliance. First, current regulations and prior rulings permit, but do not require, the use of accrual accounting for vacation pay, and they do not specify the amount to be accrued if accrual is elected; of three contractors with identical vacation plans, one may elect to recognize vacation costs pro-rata as the related work is performed, the second in the year the related work is completed, and the third only at the time vacation is taken. Consequently, current regulations do not require uniformity in the measurement of such costs among years. Second, the Internal Revenue Code and Treasury Department rulings have imposed different criteria at different times; of two contractors with identical plans, one historically may have been permitted to recognize costs of compensated personal absence on the accrual basis, while the other, who applied at a later date, is denied the same privilege because of a subsequent ruling. Finally, a change in the Internal Revenue Code or income tax regulations may not be appropriate for contract cost accounting.

Many commentators said that they were not aware of problems relating to accounting for costs of compensated personal absence and they questioned the need for a Standard on the subject. Discussions with a number of these commentators disclosed, however, that they were unaware of the lack of uniformity created by the reliance of Government Procurement regulations on income tax regulations. The Board believes that the promulgation of a Standard dealing with accounting for costs of compensated personal absence is desirable to improve, and provide uniformity in, the measurement of these costs for a cost accounting period and thereby to increase the probability that the measured costs are allocated to the proper cost objectives.

(2) *Scope of the standard.* Several commentators questioned the exclusion of such costs as severance pay or group insurance from the Standard and they concluded that these costs were thereby unallowable as contract costs. This conclusion is not correct. A Standard does not define which costs are or are not allowable. Moreover, these costs were excluded from this Standard because our research disclosed that the associated accounting problems are sufficiently dissimilar from those of compensated personal absence to warrant separate consideration.

(3) *Basis for recognition of cost.* The Standard that was published for public comment relied on the degree of certainty of the employer's obligation as the principal criterion for accrual or nonaccrual of costs of compensated personal absence. Some commentators suggested that costs not be recognized prior to payment unless the obligation to provide the benefits were irrevocable in all circumstances. Using this test, most company benefit plans which we have seen in the course of our research would not qualify for accrual accounting. Others suggested that the Standard set no restrictions whatsoever on the use of accrual accounting for these costs.

After considering all of the comments and after additional staff research and discussions with contractors, Government agencies, and others, the Board has concluded that the distinction which it previously stated between a "certain" and a "reasonably certain" obligation for purposes of determining liability, was unnecessary. The Standard has been simplified to state directly that the proper measure of the liability and the criterion for cost recognition is the amount which would be payable if the employer were to terminate the employment for any reason not involving disciplinary action. Under generally accepted accounting principles, liabilities are usually recorded when obligations to transfer assets or provide services in the future are incurred. If the employee would be paid a given amount in the event of lay-off, then that employee must have completed the service necessary to have earned that amount of entitlement to benefits.

Some commentators suggested that only so much of the employer's liability as would be payable on voluntary termination be considered to be "earned." The Board does not accept this position. Even in cases where voluntary termination causes a forfeiture, the employer cannot unilaterally avoid the liability. The employer's liability should not be disregarded merely because an employee may later act to relieve the employer of actually making the payment.

Even if the obligation is viewed as one of a contingent nature, generally accepted accounting principles provide that where the outcome is reasonably foreseeable and the contingency may be expected to result in a cost, it should be reflected in the accounts. Based on its research, the Board believes that only a small percentage of those employees of any contractor who are entitled to benefits forfeit those benefits. Therefore, the Board believes that the obligation should properly be recognized (with appropriate adjustment for anticipated forfeitures), and to fail to do so is to misstate the costs of compensated personal absence which are properly assignable to that cost accounting period.

(4) *Utilization of benefits criterion.* A number of commentators objected to the provision in the proposed Standard that if the employer's obligation were not "certain," then accrual accounting could be used only if at least 80 percent of the entitlement which was potentially earned in any year would ultimately be used by the employees. The intent of this provision was to assure that accrual accounting was not permitted in situations where the utilization rate was so low that it was questionable whether accruals based on estimated utilization provided any better cost accounting information than did actual cash disbursements. The Board has reviewed the utilization data of a number of contractors and finds that by adhering to the amount which is payable on involuntary termination of employment as the measure of the accrual, a utilization criterion is unnecessary. It has therefore been deleted.

(5) *Adjustments for unrecognized liabilities.* The Standard requires the recognition of costs when the entitlement to compensated personal absence is earned. Initial application of the Standard or a change of compensated personal absence plan may necessitate an adjustment to recognize the cost of entitlement already earned but not yet recognized for cost accounting purposes. The proposed Standard made no explicit provision for the disposition of such adjustments. A number of commentators cited the failure to provide explicitly for the disposition of adjustments as a deficiency in the proposed Standard. For example, it was hypothesized that a contractor who was recording vacation costs at the time of payment might not recognize any vacation cost in the year an employee was hired; on the completion of the contract, the employee might be terminated and paid for both the vacation to be taken in the year of termination and the vacation earned in that year. If the Standard were applicable to the contractor, he might be able to allocate only those costs accrued in that year. As a result, he might not recover costs paid in that year for vacations earned before accrual was instituted. The Board recognizes the validity of this hypothesis in some instances. However, if the contractor is viewed as a going concern and Government contracting as a continuing process, then that hypothetical "last year

of contracting" may be infinitely far in the future, the lay-offs may never take place, and the contractor will continue to receive "one year's worth of costs" in each year.

All commentators who questioned the method of adjustment, and certain other contractors who did not raise the question but who the Board believed might be significantly affected by the Standard, were asked to provide detailed information concerning benefit plans involved, the number of employees, and the estimated amount of the adjustment. In addition, each contractor was asked to provide background information concerning its history as a Government contractor and, to the extent available, data on past employment, labor costs, and extent of contracts. The Board also contracted several contractors who already record costs of compensated personal absence on the accrual basis to determine the circumstances under which this accounting treatment had been adopted, whether adoption resulted in adjustment and, if so, how it had been handled.

The Board reviewed the information submitted in response to its requests. The Board has considered (1) refraining from explicitly providing for handling the adjustment, (2) providing a procedure by which the adjustment could all be assigned to the year of change, and (3) providing a procedure for amortizing the adjustment over a fixed period of years. The Board finds disadvantages to each of these alternatives. If no procedure for adjustment is provided, appropriate procedures for cost recovery may not be devised by contracting parties. If the procedure resulted in assignment of the entire adjustment to the year of change, then some contractors may recover more than the appropriate cost of that year and all of the contracts in the year of change will be overcharged. The same deficiencies, albeit to a lesser extent, exist if the procedure provides for the adjustment to be amortized over a fixed period.

The Standard has been revised to provide an explicit procedure for disposing of the adjustment for unrecognized liability. Under it, the adjustment is initially placed in a suspense account. In the cost accounting period of change and in any subsequent period, if the employer's liability for compensated personal absence under the related plan at the end of a period is less than the amount in the suspense account at the beginning of that period, the suspense account is reduced by the amount of the difference. That difference is assigned to that cost accounting period as an additional cost of compensated personal absence.

If the employer's liability remains above that at the time of change, then costs of compensated personal absence are measured on the accrual basis. If the employer's liability falls below that amount because of additional cash payments to employees, then the costs are measured on the cash basis. This latter condition will arise whenever employment levels fall below that existing at the time of change. Whenever such conditions occur, the costs of those periods are measured on a cash basis until the entire suspense has been written off. The contractor is not precluded from allocating costs which might otherwise have been allocable, absent the Standard but he cannot allocate more than he otherwise would have allocated, so that premature cost allocations cannot occur.

(6) *Complexity.* Many of the commentators suggested that the proposed Standard was too complex, too detailed, or too procedural. As previously mentioned, the criteria for accrual have been changed to eliminate the distinction between a "certain" and a "reasonably certain" obligation and to eliminate the utilization test. These changes permitted a significant reduction in the length and complexity of the Standard. In addition, the Board has made a number of simplifying changes in the wording of the Standard based on suggestions from commentators.

(7) *Adjustments for interim rates.* A number of commentators objected to the requirement in the proposed Standard that where costs of compensated personal absence are allocated using an interim rate, any difference between the interim rate and actual cost must be adjusted in the same period. They objected on the grounds

that the necessary computations to determine the actual cost in accordance with the provisions of the Standard could not be completed by the end of the cost accounting period. Although the Board is not persuaded by this argument, the provision involved has been deleted for the following reasons. The accrual required by this Standard is identical to that required for any other year-end accrual, and the adjustment process is not essentially different from that which is required to adjust any interim allocation for a cost difference.

The requirement is well established that if overhead costs are allocated to Government contracts on an interim basis, there must be an adjustment when the actual costs are known. The Board therefore has concluded that it is unnecessary to restate it in the Standard, although the requirement, of course, remains in effect.

(8) *Requirement to maintain records.* Some contractors were concerned about the nature and extent of records which might be necessary to support the determinations and computations required by the proposed Standard. In particular, the need to maintain records of benefit utilization was questioned. The benefit utilization criterion has been deleted from the Standard; consequently, the maintenance of special records for this purpose is unnecessary. Others were concerned that the proposed Standard would require changes in their formal accounting records. Upon further consideration, the Board believes maintaining appropriate records is implicit in cost accounting and that the inclusion of additional record-keeping requirements in the Standard is unnecessary. In determining what records are necessary to achieve verifiability for purposes of this Standard, consideration should be given to the relative ease or difficulty of making and verifying assumptions and estimates, to the materiality of the amounts involved, and to the use of techniques such as statistical sampling for determining the amount of the employer's liability.

(9) *Exemptions.* Representatives of educational institutions pointed out two problems with the proposed Standard. First, it required that where costs of compensated personal absence are allocated using an interim rate, any difference between the interim rate and actual cost must be adjusted in the same period. These commentators pointed out that Pub. L. 87-638 authorized use of negotiated predetermined overhead rates by these institutions and that this permission is presently set forth in Federal Management Circular 73-8: Cost Principles for Educational Institutions. Second, they pointed out that many educational institutions do not record costs on an accrual basis; but use fund accounting on a cash basis; and that for state and local governmental institutions, such accounting may be required by law. While the Standard does not require any change in the formal accounting records, in many instances it would be very difficult for these institutions to comply with the Standard.

In view of the foregoing, the Board does not believe it desirable to require educational institutions or state and local governmental agencies to account for costs of compensated personal absence on the accrual basis. Accordingly, the Board has exempted such institutions and state and local governmental agencies from the provisions of this Standard.

(10) *Costs and benefits.* The anticipated benefits of this Standard are improved cost measurement and increased uniformity in accounting for costs of compensated personal absence, leading to increased assurance that the measured costs are assigned to the proper cost objectives.

Several commentators objected that the Standard would not increase uniformity because the accounting for a particular benefit plan would depend on the provisons of that plan, and not all benefit plans are alike. The Board is aware of the diversity of benefit plans. However, under present procurement regulations different contractors with essentially similar plans could be accounting differently for them and may be prevented from using similar accounting even if they wish to do so. To the extent that uniformity is thus actually inhibited, the Standard will correct the situation. Other past problems relating to the measurement of these costs in the event of layoffs, or employe transfers would also be alleviated.

Many commentators said that they were already accounting for costs of compensated personal absence in the manner required by the Standard. Some commentators said that implementation costs would depend on the extent of detail which would be required to comply. The Board has attempted to minimize such detail: First, by its previous statements that compliance with Standards may be accomplished through the use of memorandum records; second, by eliminating the utilization of benefits test and, thereby, the necessity of maintaining the supporting utilization records; and, finally, by emphasizing the acceptability of estimates based on statistical sampling or historical data. As a consequence, the costs of implementation should be negligible.

In summary, the Board believes that the benefits to be derived from this Standard clearly outweigh any costs of implementation.

The Board expects that this Standard will become effective on April 1, 1975.

PREAMBLE B

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised §§ 408.10 and 408.70. This amendment was part of a publication which added § 331.30 (b)(3). Only the protion of the preamble which describes the revision to §§ 408.10, 408.70 are printed here. The remainder of the preamble appears as Preamble K of the supplement to Part 331.

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In the FEDERAL REGISTER of February 15, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 409—COST ACCOUNTING STANDARD—DEPRECIATION OF TANGIBLE CAPITAL ASSETS

Sec.
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AUTHORITY: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

SOURCE: 40 FR 4264, Jan. 29, 1975, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (40 FR 4259, January 29, 1975) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 409.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

[43 FR 24820, June 8, 1978]

PREAMBLES: For preamble to § 409.10, see preamble B of the supplement to this part. For preamble to superseded regulations, see preamble A of the supplement.

§ 409.20 Purpose.

The purpose of this Standard is to provide criteria and guidance for assigning costs of tangible capital assets to cost accounting periods and for allocating such costs in cost objectives within such periods in an objective and consistent manner. The Standard is based on the concept that depreciation costs identified with cost accounting periods and benefiting cost objectives within periods should be a reasonable measure of the expiration of service potential of the tangible assets subject to depreciation. Adherence to this Standard should provide a systematic and rational flow of the costs of tangible capital assets to benefited cost objectives over the expected service lives of the assets. This Standard does not cover nonwasting assets or natural resources which are subject to depletion.

§ 409.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Residual value.* The proceeds (less removal and disposal costs, if any) realized upon disposition of a tangible capital asset. It usually is measured by the net proceeds from the sale or other disposition of the asset, or its fair value if the asset is traded in on another asset. The estimated residual value is a current forecast of the residual value.

(2) *Service life.* The period of usefulness of a tangible capital asset (or group of assets) to its current owner. The period may be expressed in units of time or output. The estimated service life of a tangible capital asset (or group of assets) is a current forecast of its service life and is the period over which depreciation cost is to be assigned.

(3) *Tangible capital asset.* An asset that has physical substance, more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the services it yields.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 409.40 Fundamental requirement.

(a) The depreciable cost of a tangible capital asset (or group of assets) shall be assigned to cost accounting periods in accordance with the following criteria:

(1) The depreciable cost of a tangible capital asset shall be its capitalized cost less its estimated residual value.

(2) The estimated service life of a tangible capital asset (or group of assets) shall be used to determine the cost accounting periods to which the depreciable cost will be assigned.

(3) The method of depreciation selected for assigning the depreciable cost of a tangible capital asset (or group of assets) to the cost accounting periods representing its estimated service life shall reflect the pattern of consumption of services over the life of the asset.

(4) The gain or loss which is recognized upon disposition of a tangible capital asset shall be assigned to the cost accounting period in which the disposition occurs.

(b) The annual depreciation cost of a tangible capital asset (or group of assets) shall be allocated to cost objectives for which it provides service in accordance with the following criteria:

(1) Depreciation cost may be charged directly to cost objectives only if such charges are made on the basis of usage and only if depreciation costs of all like assets used for similar purposes are charged in the same manner.

(2) Where tangible capital assets are part of, or function as, an organizational unit whose costs are charged to other cost objectives based on measurement of the services provided by the organizational unit, the depreciation cost of such assets shall be included as part of the cost of the organizational unit.

(3) Depreciation costs which are not allocated in accordance with paragraph (b) (1) or (2) of this section, shall be included in appropriate indirect cost pools.

(4) The gain or loss which is recognized upon disposition of a tangible capital asset, where material in amount, shall be allocated in the same manner as the depreciation cost of the asset has been or would have been al-

located for the cost accounting period in which the disposition occurs. Where such gain or loss is not material, the amount may be included in an appropriate indirect cost pool.

§ 409.50 Techniques for application.

(a) Determination of the appropriate depreciation charges involves estimates both of service life and of the likely pattern of consumption of services in the cost accounting periods included in such life. In selecting service life estimates and in selecting depreciation methods many of the same physical and economic factors should be considered. The following are among the factors which may be taken into account: Quantity and quality of expected output, and the timing thereof; costs of repair and maintenance, and the timing thereof; standby or incidental use and the timing thereof; and technical or economic obsolescence of the asset (or group of assets), or of the product or service it is involved in producing.

(b) Depreciation of a tangible capital asset shall begin when the asset and any others on which its effective use depends are ready for use in a normal or acceptable fashion. However, where partial utilization of a tangible capital asset is identified with a specific operation, depreciation shall commence on any portion of the asset which is substantially completed and used for that operation. Depreciable spare parts which are required for the operation of such tangible capital assets shall be accounted for over the service life of the assets.

(c) A consistent policy shall be followed in determining the depreciable cost to be assigned to the beginning and ending cost accounting periods of asset use. The policy may provide for any reasonable starting and ending dates in computing the first and last year depreciable cost.

(d) Tangible capital assets may be accounted for by treating each individual asset as an accounting unit, or by combining two or more assets as a single accounting unit, provided such treatment is consistently applied over the service life of the asset or group of assets.

(e) Estimated service lives initially established for tangible capital assets (or groups of assets) shall be reasonable approximations of their expected actual periods of usefulness, considering the factors mentioned in paragraph (a) of this section. The estimate of the expected actual periods of usefulness need not include the additional period tangible capital assets are retained for standby or incidental use where adequate records are maintained which reflect the withdrawal from active use.

(1) The expected actual periods of usefulness shall be those periods which are supported by records of either past retirement or, where available, withdrawal from active use (and retention for standby or incidental use) for like assets (or groups of assets) used in similar circumstances appropriately modified for specifically identified factors expected to influence future lives. The factors which can be used to modify past experience include:

(i) Changes in expected physical usefulness from that which has been experienced such as changes in the quantity and quality of expected output.

(ii) Changes in expected economic usefulness, such as changes in expected technical or economic obsolescence of the asset (or group of assets), or of the product or service produced.

(2) Supporting records shall be maintained which are adequate to show the age at retirement or, if the contractor so chooses, at withdrawal from active use (and retention for standby or incidental use) for a sample of assets for each significant category. Whether assets are accounted for individually or by groups, the basis for estimating service life shall be predicated on supporting records of experienced lives for either individual assets or any reasonable grouping of assets as long as that basis is consistently used. The burden shall be on the contractor to justify estimated service lives which are shorter than such experienced lives.

(3) The records required in paragraphs (e) (1) and (2) of this section, if not available on the date when the requirements of this Standard must first be followed by a contractor, shall be

developed from current and historical fixed asset records and be available following the second fiscal year after that date. They shall be used as a basis for estimates of service lives of tangible capital assets acquired thereafter. Estimated service lives used for financial accounting purposes (or other accounting purposes where depreciation is not recorded for financial accounting purposes for some noncommercial organizations), if not unreasonable under the criteria specified in paragraph (e) of this section, shall be used until adequate supporting records are available.

(4) Estimated service lives for tangible capital assets for which the contractor has no available data or no prior experience for similar assets shall be established based on a projection of the expected actual period of usefulness, but shall not be less than asset guideline periods (mid-range) estaboished for asset guideline classes under the Revenue Procedure 72-10 published by the Internal Revenue Service, and any additions, supplements or revisions thereto, which are in effect as of the first day of the cost accounting period in which the assets are acquired. Use of this alternative procedure shall cease as soon as the contractor is able to develop estimates which are appropriately supported by his own experience.

(5) The contracting parties may agree on the estimated service life of individual tangible capital assets where the unique purpose for which the equipment was acquired or other special circumstances warrant a shorter estimated service life than the life determined in accordance with the other provisions of this § 409.50(e) and where the shorter life can be reasonably predicted.

(f) (1) The method of depreciation used for financial accounting purposes (or other accounting purposes where depreciation is not recorded for financial accounting purposes) shall be used for contract costing unless (i) such method does not reasonably reflect the expected consumption of services for the tangible capital asset (or group of assets) to which applied, or (ii) the method is unacceptable for Federal income tax purposes. If the contractor's method of depreciation used for financial accounting purposes (or other accounting purposes as provided above) does not reasonably reflect the expected consumption of services or is unacceptable for Federal income tax purposes, he shall establish a method of depreciation for contract costing which meets these criteria, in accordance with paragraph (f)(3) of this section.

(2) After the date of initial applicability of this Standard, selection of methods of depreciation for newly acquired tangible capital assets, which are different from the methods currently being used for like assets in similar circumstances, shall be supported by projections of the expected consumption of services of those assets (or groups of assets) to which the different methods of depreciation shall apply. Support in accordance with paragraph (f)(3) of this section shall be based on the expected consumption of services of either individual assets or any reasonable grouping of assets as long as the basis selected for grouping assets is consistently used.

(3) The expected consumption of asset services over the estimated service life of a tangible capital asset (or group of assets) is influenced by the factors mentioned in paragraph (a) of this section which affect either potential activity or potential output of the asset (or group of assets). These factors may be measured by the expected activity or the expected physical output of the assets, as for example: Hours of operation, number of operations performed, number of units produced, or number of miles traveled. An acceptable surrogate for expected activity or output might be a monetary measure of that activity or output generated by use of tangible capital assets, such as estimated labor dollars, total cost incurred or total revenues, to the extent that such monetary measures can reasonably be related to the usage of specific tangible capital assets (or groups of assets). In the absence of reliable data for the measurement or estimation of the consumption of asset services by the techniques mentioned, the expected consumption of services may be represented by the passage of time. The appropriate

method of depreciation should be selected as follows:

(i) An accelerated method of depreciation is appropriate where the expected consumption of asset services is significantly greater in early years of asset life.

(ii) The straight-line method of depreciation is appropriate where the expected consumption of asset services is reasonably level over the service life of the asset (or group of assets).

(g) The estimated service life and method of depreciation to be used for an original complement of low-cost equipment shall be based on the expected consumption of services over the expected useful life of the complement as a whole and shall not be based on the individual items which form the complement.

(h) Estimated residual values shall be determined for all tangible capital assets (or groups of assets). For tangible personal property, only estimated residual values which exceed ten percent of the capitalized cost of the asset (or group of assets) need be used in establishing depreciable costs. Where either the declining balance method of depreciation or the class life asset depreciation range system is used consistent with the provisions of this Standard, the residual value need not be deducted from capitalized cost to determine depreciable costs. No depreciation cost shall be charged which would significantly reduce book value of a tangible capital asset (or group of assets) below its residual value.

(i) Estimates of service life, consumption of services, and residual value shall be reexamined for tangible capital assets (or groups of assets) whenever circumstances change significantly. Where changes are made to the estimated service life, residual value, or method of depreciation during the life of a tangible capital asset, the remaining depreciable costs for cost accounting purposes shall be limited to the undepreciated cost of the assets and shall be assigned only to the cost accounting period in which the change is made and to subsequent periods.

(j) (1) Gains and losses on disposition of tangible capital assets shall be considered as adjustments of depreciation costs previously recognized and shall be assigned to the cost accounting period in which disposition occurs except as provided in paragraphs (j) (2) and (3) of this section. The gain or loss for each asset disposed of is the difference between the net amount realized, including insurance proceeds in the event of involuntary conversion, and its undepreciated balance. However, the gain to be recognized for contract costing purposes shall be limited to the difference between the original acquisition cost of the asset and its undepreciated balance.

(2) Gains and losses on the disposition of tangible capital assets shall not be recognized where:

(i) Assets are grouped and such gains and losses are processed through the accumulated depreciation account, or, (ii) the asset is given in exchange as part of the purchase price of a similar asset and the gain or loss is included in computing the depreciable cost of the new asset. Where the disposition results from an involuntary conversion and the asset is replaced by a similar asset, gains and losses may either be recognized in the period of disposition or used to adjust the depreciable cost base of the new asset.

(3) The contracting parties may account for gains and losses arising from mass or extraordinary dispositions in a manner which will result in treatment equitable to all parties.

(4) Gains and losses on disposition of tangible capital assets transferred in other than an arms-length transaction and subsequently disposed of within 12 months from the date of transfer shall be assigned to the transferor.

(k) Where, in accordance with § 409.40(b)(1), the depreciation costs of like tangible capital assets used for similar purposes are directly charged to cost objectives on the basis of usage, average charging rates based on cost shall be established for the use of such assets. Any variances between total depreciation cost charged to cost objectives and total depreciation cost for the cost accounting period shall be accounted for in accordance with the contractor's established practice for handling such variances.

(l) Practices for determining depreciation methods, estimated service lives and estimated residual values need not be changed for assets acquired prior to compliance with this Standard if otherwise acceptable under applicable procurement regulations. However, if changes are effected such changes must conform to the criteria established in this Standard and may be effected on a prospective basis to cover the undepreciated balance of cost by agreement between the contracting parties pursuant to negotiation under (a)(4)(B) or (C) of the Contract Clause set out as § 331.50 of the Board's regulations (4 CFR 331.50).

[40 FR 4264, Jan. 29, 1975; 40 FR 8321, Feb. 27, 1975, as amended at 43 FR 9781, Mar. 10, 1978; 43 FR 16149, Apr. 17, 1978]

Preamble: For preamble relating to § 409.50, see preamble J of the supplement to Part 331.

§ 409.60 Illustrations.

The following examples are illustrative of the provisions of this Standard.

(a) X, Y, and Z companies purchase identical milling machines to be used for similar purposes.

(1) Company X estimates service life for tangible capital assets on a individual asset basis. Its experience with similar machines is that the average replacement period is 14 years. Under the provisions of the Standard, Company X shall use the estimated service life of 14 years for the milling machine unless it can demonstrate changed circumstances or new circumstances to support a different estimate.

(2) Company Y estimates service life for tangible capital assets by grouping assets of the same general kind and with similar service lives. Accordingly, all machine tools are accounted for as a single group. The average replacement life for machine tools for Company Y is 12 years. In accordance with the provisions of the Standard, Company Y shall use a life of 12 years for the acquisition unless it can support a different estimate for the entire group.

(3) Company Z estimates service life for tangible capital assets by grouping assets according to use without regard to service lives. Accordingly, all machinery and equipment is accounted for as a single group. The average replacement life for machinery and equipment in Company Z is ten years. In accordance with the provisions of the Standard, Company Z shall use an estimated service life of ten years for the acquisition unless it can support a different estimate for the entire group.

(b) Company X desires to charge depreciation of the milling machine described in paragraph (a) of this section, directly to final cost objectives. Usage of the milling machine can be measured readily based on hours of operation. Company X may charge depreciation cost directly on a unit of time basis provided he uses one depreciation charging rate for all like milling machines in the machine shop and charges depreciation for all such milling machines directly to benefiting cost objectives.

(c) A contractor acquires, and capitalizes as an asset accountability unit, a new lathe. The estimated service life is ten years for the lathe. He acquires, and capitalizes as an original complement of low-cost equipment related to the lathe, a collection of tool holders, chucks, indexing heads, wrenches, and the like. Although individual items comprising the complement have an average life of six years, replacements of these items will be made as needed and, therefore, the expected useful life of the complement is equal to the life of the lathe. An estimated service life of ten years should be used for the original complement.

(d) A contractor acquires a test facility with an estimated physical life of ten years, to be used on contracts for a new program. The test facility was acquired for $5 million. It is expected that the program will be completed in six years and the test facility acquired is not expected to be required for other products of the contractor. Although the facility will last ten years, the contracting parties may agree in advance to depreciate the facility over six years.

(e) Contractor acquires a building by donation from its local Government. The building had been purchased new by another company and subsequently acquired by the local Government. Contractor capitalizes the building at its fair value. Under the Standard the depreciable cost of the asset based on that value may be accounted for over its estimated service life and allocated to cost objectives in accordance with contractor's cost allocation practices.

(f) A major item of equipment which was acquired prior to the applicability of this Standard was estimated, at acquisition, to have a service life of 12 years and a residual value of no more than 10 percent of acquisition cost. After four years of service, during which time this Standard has become applicable, a change in the production situation results in a well-supported determination to shorten the estimated service life to a total of seven years. The revised estimated residual value is 15 percent of acquisition cost. The annual depreciation charges based on this particular asset will be appropriately increased to amortise the remaining cost, less the current estimate of residual value, over the remaining three years of expected usefulness. This change is not a change of cost accounting practice, but a correction of numeric estimates. The requirement of § 409.50(1) for an adjustment pursuant to section (a)(4)(B) or (C) of the CAS clause does not apply.

(g) The support required by § 409.50(e) can, in all likelihood, be derived by sampling from almost any reasonable fixed asset records. Of course, the more complete the data in the records which are available, the more confidence there can be in determinations of asset service lives. The following descriptions of sampling methods are illustrations of techniques which may be useful even with limited fixed asset records.

(1) A company maintains an inventory of assets in use. The company should select a sampling time period which, preferably, is significantly longer than the anticipated life of the assets for which lives are to be established. Of course, the inventory must be available for each year in the sampling time period. The company would then select a random sample of items in each year except the most recent year of the time period. Each item in the sample would be compared to the subsequent year's inventory to determine if the asset is still in service; if not, then the asset had been retired in the year from which the sample was drawn. The item is then traced to prior year inventories to determine the year in which acquired.

NOTE: Sufficient items must be drawn in each year to assure an adequate sample.

(2) A company maintains an inventory of assets in use and also has a record of retirements. In this case the company does not have to compare the sample to subsequent years to determine if disposition has occurred. As in Example (1) above the sample items are traced to prior years to determine the year in which acquired.

(3) A company maintains retirement records which show acquisition dates. The company should select a sampling time period which, preferably, is significantly longer than the anticipated life of the assets for which lives are to be estimated. The company would then select a random sample of items retired in each year of the sampling time period and tabulate age at retirement.

(4) A company maintains only a record of acquisitions for each year. The company should select a random sample of items acquired in the most recent complete year and determine from current records or observations whether each item is currently in service. The acquisitions of each prior year should be sampled in turn to determine if sample items are currently in service. This sampling should be performed for a time period significantly longer than the anticipated life of assets for which the lives are to be established, but can be discontinued at the point at which sample items no longer appear in current use. From the data obtained, mortality tables can be constructed to determine average asset life.

(5) A company does not maintain accounting records on fully depreciated assets. However, property records are maintained, and such records are retained for three years after disposition of an asset in groups by year of disposition. An analysis of these retirements may be made by selecting the larger dollar items for each category of assets for which lives are to be determined (for example, at least 75 percent of the acquisition values retired

each year). The cases cited above are only examples and many other examples could have been used. Also, in any example, a company's individual circumstances must be considered in order to take into account possible biased results because of changes in organizations, products, acquisition policies, economic factors, etc. The results from example (g)(5) of this section, for instance, might be substantially distorted if the three year period was unusual with respect to dispositions. Therefore, the examples are illustrative only and any sampling performed in compliance with this Standard should take into account all relevant information to assure that reasonable results are obtained.

[40 FR 4264, Jan. 29, 1975; 40 FR 8321, Feb. 27, 1975, as amended at 43 FR 9781, Mar. 10, 1978]

PREAMBLE: For preamble relating to § 409.60, see preamble J of the supplement to Part 331.

§ 409.70 Exemption.

This Standard shall not apply where compensation for the use of tangible capital assets is based on use allowances as provided for by the provisions of Federal Management Circular 73-8 (Cost Principles for Educational Institutions), Federal Management Circular 74-4 (Principles for Determining Costs Applicable to Grants and Contracts with State and Local Governments), or other appropriate Federal procurement regulations.

§ 409.80 Effective date.

(a) The effective date of this Cost Accounting Standard is July 1, 1975.

(b) This Cost Accounting Standard shall be followed by each contractor for all tangible capital assets acquired on or after the start of his next fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

[40 FR 4264, Jan. 29, 1975, as amended at 40 FR 15865, Apr. 8, 1975]

PREAMBLE: For an explanation of how effective dates are determined, see preamble A of the supplement to Part 401 of this chapter.

PREAMBLE A

Preamble to Original Publication, 1-29-75

The following is the preamble to the original publication of Part 409, 40 FR 4259, Jan. 29, 1975.

The Standards on Depreciation of Tangible Capital Assets being published today is one of a series being promulgated by the Cost Accounting Standards Board (CASB) pursuant to sec. 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

On February 27, 1973, the Board promulgated a Standard on Capitalization of Tangible Assets. At that time the Board described its work to date in the area of fixed asset accounting including studies of practices used for both capitalization and depreciation. The responses to an issues paper and a questionnarie which were used in the development of the capitalization Standard were also useful in the development of the Standard being promulgated today. A preliminary draft of the Cost Accounting Standard on Depreciation of Tangible Capital Assets was widely distributed in March 1973 for informal comment by interested parties. The Board's further consideration of the issues related to depreciation has been significantly enhanced by the responses received from well over 100 respondents to that informal proposal.

The Board's research into fixed asset accounting practices included a survey of 107 profit centers selected to be representative of the diversity of firms to which Cost Accounting Standards apply. Reports on their fixed asset accounting practices and statistical information for a five-year period were received and analyzed. The Board was assisted in its deliberation by information available from the 1960 Treasury Department Survey which provided the data base for the "Asset Guideline Lives" used in Revenue Procedure 62-21 and data developed in an accounting research study performed for the American Institute of Certified Public Accountants.

A proposed Cost Accounting Standard dealing with depreciation was published by the Board on June 11, 1974 (39 FR 20505). After reviewing the responses to that publication, the Board revised its proposal. The revised version was published in the FEDERAL REGISTER for October 3, 1974 (39 FR 35678). The Board supplemented both FEDERAL REGISTER publications by sending copies of the FEDERAL REGISTER material directly to organizations and individuals who were expected to be interested. The Board received almost 200 responses to the June 11 and the October 3 proposals. Comments were received from individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and individuals. All of these comments have been carefully considered by the Board. In addition, the Board invited representatives of Government agencies, professional accounting and industry associations, and defense contractors to attend Board meetings and discuss their views on the significant issues concerning depreciation practices in Government contract costing. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by organizations and individuals have resulted in many changes in the Standard.

The comments below summarize the major issues discussed by respondents in connection with both preliminary publications. They explain the major changes which have been made since the June 11 proposal.

(1) *Economic Impact of the Standard.* Many of the comments on the June 11 and October 3 proposals were concerned with the economic impact of the Standard. They cited such concerns as delays in cash flow, impact of inflation, incentives for modernization, and administrative cost of additional recordkeeping requirements.

The Board's consideration of each of these primary concerns is dealt with in detail in other sections of these prefatory comments. The Board has recognized the potential overall impact of the Standard as expressed in the comments received and has endeavored to establish the needed guidance on depreciation accounting with as little disruption as possible to contractors and current contractual relationships.

The Standard provides for a phasing in of requirements over a period of time so that the principal impact of the Standard will be a number of years in the future. The Standard applies only to assets acquired by a contractor after the beginning of its next fiscal year after receipt of a CAS covered contract. If the Standard were to become effective six months after submission to Congress, application of any provisions of the Standard to any newly acquired assets would be delayed more than six months from date of promulgation and for most contractors at least 12 months.

The Standard provides for a two-year period to develop records on past experience to support estimates of service lives. The same period could be used to develop any necessary changes in accounting for fixed asset lives. The two-year period begins after required compliance with the Standard, and, therefore, most contractors would have at least three years in which to apply the recordkeeping provisions for newly acquired fixed assets.

For those contractors who use the two-year period to develop new estimated service lives, the effect of the use of those new estimates would begin on assets acquired in the fourth year after submission of this Standard to Congress. In the fourth year and the next several years thereafter the impact of changes in cash flow because of changes in service life estimates would be minimal, since the difference in cash flow each year is the difference between depreciation amounts under the old and new estimates of service life for the newly acquired assets. The total impact on cash flow of changes in estimates of service life would not occur until the full cycle of asset replacement is completed. In addition, the impact of the rules on accounting for gain or loss would only begin to take place where new assets acquired after compliance with the Standard would be sold or otherwise disposed of and such impact will be many years in the future.

It is the Board's opinion that the immediate economic and administrative impact of the Standard is minimal and will, over time, provide for a more appropriate recognition of cost accounting considerations distinct and apart from profit level determinations for defense contract cost and pricing actions.

(2) *Need for a Standard.* The accounting profession has established general principles to govern depreciation accounting. These broad principles require that depreciation practices be systematic and rational. Accountants consistently urge that the estimates of service lives used for depreciation should be realistic. These broad goals are almost universally agreed upon.

Some commentators suggested that the Board should not promulgate any Standard dealing with depreciation because the applicable principles have been well established as a part of generally accepted accounting principles. These same commentators also argue that procurement regulations have allowed contractors to rely on depreciation practices found to be acceptable for other purposes; they believe that contract costing should continue to rely entirely upon the depreciation practices used for Federal income tax and for financial reporting purposes pursuant to the current procurement regulations. The Board believes, however, that depreciation charges based entirely on income tax and financial reporting practices do not necessarily assure reasonable representation of the costs of the services provided on Government contracts.

Various mathematical formulas have been suggested to represent the typical patterns of consumption of services over the lives of assets. Certain of these methods of depreciation have been incorporated into the Internal Revenue Code as acceptable for Federal income tax purposes. These same methods have, in general, been accepted as systematic and rational and therefore within the scope of generally accepted accounting principles. The Board finds that there has been a range of choice as to depreciation methods available for contract costing, without adequate criteria for the choices made.

The Treasury Department and Internal Revenue Service have established guidelines for determination of estimated periods of useful service. These guideline periods are said to be based on observed industry experience, but lives shorter than the averages experienced were established so that most companies would experience longer actual asset utilization periods than the permitted tax lives. Tax accounting lives for an industry are, therefore, not good representations of expected actual asset utilization periods for many individual contractors within that industry.

The Board's research has indicated that the asset lives and depreciation methods selected by defense contractors under existing regulations may result in an unduly accelerated allocation of depreciation to the final cost objectives of earlier cost accounting periods in the life of a tangible capital asset. Contractor representatives have expressed the view that the choices are typically appropriate in view of the uncertainties of Government contracting. These uncertainties, however, have not precluded utilization of assets well beyond the short estimated service lives based on the IRS guideline periods. Other commentators were concerned that any Standard which would restrict cash flow would adversely impact profits. The Board has determined that a Cost Accounting Standard is needed to provide more assurance that depreciation costs identified with performance of negotiated defense contracts are appropriately measured. Consideration of risk and capital investment in the determination of the adequacy of profits is a policy question for the procuring agencies and not a cost accounting problem.

(3) *Method of Depreciation.* Many of the comments received on depreciation method center on whether accelerated methods or straightline methods are more appropriate for contract costing purposes. The Board, however, believes that no particular method is necessarily appropriate for all contract cost accounting situations. The

Board is establishing criteria by which the method or methods appropriate in the specific situation can be determined.

Both the June 11 proposal and the October 3 revision provided that the method selected "shall reflect the expected consumption of services in each accounting period." This basic goal is generally recognized as appropriate. Commentators have raised questions relating to the practical aspects of compliance with the basic goal. What kind of evidence should be available to support a selection of a depreciation method? In the absence of authoritative criteria for selection, contractors have had no need to support their choices, nor have they accumulated much experience in collecting evidence relevant to the consumption of services. Thus a requirement for support of accelerated methods is seen by some as a prohibition of the use of such methods. However, the proposals made no distinction between an accelerated method or the straight-line method of depreciation in determining the quantity and quality of supporting evidence. The Board's proposals included descriptions of the techniques which should be used to determine appropriate methods for depreciation. The Board recognized the difficulty which might be experienced by contractors attempting to demonstrate the appropriateness of their choices. The Board's proposals included, therefore, the provision that the method of depreciation used for financial accounting purposes should generally be acceptable for contract costing.

Representatives of the accounting profession pointed out that there is strong economic motivation to choose rapid depreciation write-off techniques where cost is the basis for pricing and reimbursement, as in the defense contracting environment. They say that this same motivation may not apply to external financial accounting for the same companies. Accordingly, they expect that any Cost Accounting Standard which required that, in order to use a technique for contract costing, a company must use the same technique for financial accounting, might create an incentive to modify financial accounting practices solely for the purpose of obtaining an advantage in contract pricing. Because of these considerations the Board would prefer not to base its criteria primarily on practices used for external financial reporting.

Most commentators have asserted that the depreciation methods now in use for external reporting purposes are appropriate methods for contract costing, too. The Board believes that this is generally true, and it further recognizes that a requirement to change to a particular depreciation method might result in significant cost to many contractors. In the belief that the methods selected as appropriate for financial accounting are usually intended to approximate the actual consumption of services, the Board has provided for continuance of those methods where this is a reasonable assumption. Therefore, in the October 3 proposal the word "reasonably" was used to modify the requirement that the method of depreciation reflect the expected consumption of services; this provision is continued in the Standard being promulgated today. In those few cases where existing methods used for financial accounting purposes are obviously poor representatives of the expected pattern of consumption, and in any case when the contractor proposes to change methods, the choice should be made on the basis of a reasonable expectation of the future pattern of consumption of services in accordance with the criteria provided in this Standard.

It has been asserted that some assets purchased for Government contract purposes are used on an intermittent basis with periods of use and periods of nonuse following one another in a pattern that fits neither the classical accelerated nor straight-line models and that does not conform with the active-standby dichotomy. "The pattern of consumption of services" for such an asset is difficult to determine either prospectively or historically and is not necessarily dependent solely on use.

In circumstances such as the foregoing, it is not the intent of the Board to introduce uncertainty into contract negotiation and settlement by encouraging challenge of contractors' depreciation methods. If the method selected is also used for external financial reporting and is acceptable for income tax purposes, the Board's expectation is that it will be accepted.

(4) *Service Lives.* Depreciation is to be charged during the period of estimated usefulness of a tangible capital asset. Some commentators have expressed concern lest the Board not give appropriate recognition to the importance of possible obsolescence in estimating the period of usefulness. The Board recognizes that for many contractors the likelihood of obsolescence is an important factor in estimating the period of usefulness, and has so provided in the Standard.

The June 11 proposal provided that estimated service lives used for financial accounting, where such lives reasonably represented expected usefulness, were to be used for contract costing. However, several commentators expressed concern that the requirement to use financial accounting lives would continue to influence the motivation of some financial reporting entities to select for financial accounting purposes those practices which would be most advantageous for other purposes. The Board's research showed that defense contractors often used minimum lives permitted for tax purposes for financial accounting rather than lives based on actual experience. Therefore, the October 3 revised proposal placed the primary reliance for estimation of service lives on records of the age of assets at disposal or withdrawal from active use. The proposal further provided that the historical data would be a baseline for estimates of useful life which could be adjusted based on expected changes in physical or economic lives.

Contractors commenting on the October 3 proposal pointed out that they have not been required to have records which would show the retention periods of assets. Therefore, while most contractors have the basic information from which they could determine typical asset retention periods, few contractors have made analyses or summaries of the information available. Furthermore, they stated that contractors did not have records reflecting the withdrawal of assets from active use. The contractors expressed the opinion that to develop such records would be costly. The Standard has been modified to provide that the development of records of asset withdrawal from active use be at the option of the contractor; however, it should be pointed out that such records could be additional support to reduce historical asset lives.

The Standard also provides a two-year period for the development of analyses of historical asset lives. The Board believes the two-year period should provide adequate working time to develop such analyses. The Standard does not prescribe the nature of the analyses which should be performed, nor does it prescribe the number of prior years to be analyzed or the extent of support necessary; it recognizes that the adequacy of records depends upon individual needs and circumstances. The Board believes that most contractors have adequate records on asset retention. Estimates of experienced lives can be developed from these existing records on the basis of samples. Statistical sampling from existing records or judgmental samples with analyses to support a large portion of the dollar amounts involved may allow reasonable estimates in many cases with a relatively small sample. The Board expects that contractors will develop sufficient data to support the lives used and that procurement agencies will enforce this requirement in a reasonable manner.

Several commentators criticized the October 3 proposal on the basis that it would engender disagreements about the impact of the physical and economic factors recognized as appropriate to consider in relating actual past experience to expected future usefulness. The Board, in effect, places a burden of proof on the contractor who proposes that expected changes in physical and economic factors should be used to justify any specific reduction in estimate from that supported by his records.

The Board recognizes that many contractors would still be concerned not only about the concept of developing service life estimates from records of actual use but also about the risk of disagreements related to the appropriate adjustments to be made in relating actual past experience to expected future usefulness. The Board believes that procurement agencies generally recognize the significance of the physical and economic factors listed in the Standard. The Board encourages the procurement agencies to provide written guidance for use by field personnel, with the goal of making an effective transition from amortization periods derived from tax regulations to those based on reasonable estimates of actual useful service. The staff of the Board will participate, if requested, in the development of appropriate guidance to field personnel.

(5) *Reliance on Internal Revenue Service.* Many commentators, throughout the Board's research process in the development of this Standard, have suggested that the Board should rely on the experience accumulated by the Internal Revenue Service. Under this general approach the Board would be expected to concede that there is so much uncertainty about depreciation that auditors should not ask for support of estimates from individual contractors, but should accept for contract purposes the operation of a broad band of averages which have been developed for other purposes but which do deal with the same depreciation practices. The Board has recognized that contract costing often deals with the same expenditures and the same problems of allocation to time periods as are of interest in income tax accounting. Tax regulations, however, are intended to achieve a variety of social goals quite foreign to the purposes of contract costing. In this regard, the "Asset Guideline Periods," first established in 1962, were based on write-off periods substantially shorter than actual average experienced lives and these periods were subject to further reduction under the "Asset Depreciation Range System" in 1971.

In addition, tax assessment and collection are continuous so that, except for differences in tax rates, shifts of income or expense from one year to another generally do not have a significant effect on total tax paid over a period of time. However, similar shifts of cost from one year to another could have a decided impact on the costs chargeable to the Government on contracts with it.

The Board has considered very seriously the issues which are related to its decision not to rely solely or necessarily on I.R.S. regulations with respect to depreciation. Early versions of this Standard placed some reliance on I.R.S. regulations. However, spokesmen for contractors critized the specific techniques used, including the difficulty of using lives shorter than those permitted by I.R.S., while representatives of the accounting profession tended to encourage less reliance on I.R.S. in any way. The Standard now being promulgated continues to make limited use of I.R.S. regulations for estimating service lives where more pertinent information is not available.

(6) *Beginning and Ending Periods.* Several commentators expressed concern that the proposed Standard (both the June 11 and October 3 versions, which were alike in this regard) would not permit accounting conventions to be used for the beginning and ending periods of asset use. The Standard permits the application of conventions (such as the half-year convention) where reasonable in the circumstances and consistently followed. The Board sees no need for change in this respect.

(7) *Asset Groups.* Some commentators felt that the June 11 proposal implied a desire by the Board for depreciation accounting on an asset-by-asset basis. The Board does not intend to force any changes in decisions reasonably made with respect to accounting in terms of groups or of individual assets. Since depreciation is largely based on the application of estimates, when groups are used the estimates are intended to represent the average or typical experience for all individual assets in the group. The October 3 proposal was modified to make clear the Board's acceptance of grouping practices in accounting for assets and in determining applicable depreciation lives and methods. The Standard permits accounting for assets either individually or in any reasonable grouping, provided that the accounting treatment is consistently applied.

(8) *Use Rates.* In its June 11 proposal, the Board pointed out that the proposed Standard is expected to be applied by contractors in situations where depreciation cost is a factor in determining equitable charging rates to be used as a basis for contract costing. For example, the development of rate schedules for construction plant and equipment and ownership costs for comparison to lease or rental costs would be accomplished in conformance with the requirements of the proposed Standard. The proposed Standard also would have been required to be used by educational institutions in determining amounts to be compensated for use of buildings, capital improvements and equipment.

University commentators stated that few colleges and universities recognize depreciation in their accounting records. Replacement of capital assets is often handled by special appropriations or by bequests and other contributions. Federal Management Circular 73-8 has provided for use allowances as recognition for the employment of capital assets on contract work.

A number of commentators have pointed out that many educational institutions prefer the current use allowance system even though they recognize that conventional depreciation accounting would result in higher recognized costs. The most important reason stated is that the administrative cost and effort involved in establishing depreciation accounts would be significant.

These comments have been persuasive. Universities who choose not to incur the additional administrative expense should have an acceptable alternative basis for reimbursement for the use of tangible capital assets. The Standard has been modified to provide that it does not apply where FMC 73-8 use allowances are a part of contract costs. However, the Standard does apply whenever depreciation accounting is used by an educational institution for a covered contract.

(9) *Residual Value.* Several commentators expressed concern that the proposed Standard defined "residual value" even though the only available numeric value during the service life of an asset is that for "estimated residual value." The wording in the definition has been modified to clarify the Board's recognition of this point.

The proposal included permission to disregard minor residual values (those under ten percent of capitalized cost) in determining a schedule of depreciation charges—until the net book value approaches the residual value. Some commentators suggested that residual values be ignored completely. Others suggested that they be permitted to depreciate beyond actual residual values because of practicality considerations.

The Board has several times expressed its belief that the administration of Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. (See, for example, the March 1973 "Statement of Operating Policies, Procedures and Objectives.") Except for depreciable real property, there would usually be little improvement in the accuracy of cost measurements if estimates of minor residual values were explicitly considered in establishing amounts to be depreciated. However, the Board continues to believe that the magnitude of the expected residual value should be considered for each asset or for each group. If the estimate is greater than ten percent of capitalized cost or if it is applicable to depreciable real property it should be deducted from the capitalized amount in determining the depreciable cost. The Standard has been modified to clarify the applicability of the ten percent materiality rule to personal property only.

The June 11 proposal prohibited the charging of any depreciation amount which would reduce book value below residual value. Where fixed asset accounting is by groups, this provision was not intended to require separate identification of the book values and residual values of individual assets. For individual assets, where actual residual values are not material, the Board does not intend that such immaterial amounts be identified. The criterion of materiality applies to all Board promulgations, and therefore, the Board does not believe it necessary to restate it in every circumstance.

(10) *Gain or Loss*. Both the June 11 and October 3 proposals required that gain or loss on disposition of tangible capital assets be assigned to the cost accounting period in which disposition occurs. A number of commentators suggested that gain or loss on disposition, as an adjustment of depreciation previously recognized, should be assigned to the cost accounting periods and cost objectives to which the depreciation had been charged. This suggestion is conceptually sound but impractical to apply. The records necessary to identify prior depreciation charges would be difficult to maintain. In addition, where losses occur on disposition, application of the cost to prior periods and cost objectives would often be precluded because applicable contracts may have been closed or funding for the additional cost may not be available. Accordingly, the Board believes it would be fair to both contractors and the Government to adjust for gain or loss in the current cost accounting period.

Commentators suggested that if adjustment is to be made in the current cost accounting period, it should be made to some general indirect cost pool so that adjustments could be absorbed by all work of the period. The Board believes, however, that—to the extent practical—adjustments should be made to the same cost accounts to which the depreciation cost of the asset had been or would have been allocated in that cost accounting period. To the extent that depreciation cost is assigned to individual departments or cost centers, so should the adjustments to depreciation resulting from the disposition of assets.

Commentators expressed the opinion that gains on disposition of assets in today's economy are often the result of inflation and not adjustments of depreciation expense. The Board recognizes that assets held for long periods, especially real property, may be disposed of for amounts in excess of net book value. The gain may have been caused by any of several factors, including the rising general price level. In some situations it may be arguable that the gains should not be considered as corrections to previous depreciation charges. The Board and others in the accounting profession are examining new techniques to deal with accounting for inflation. However, accounting for cost on an historical basis is now generally accepted and until the new techniques are developed and accepted, the Board does not see a practical way to differentiate those gains deemed by some to be based on inflation from those resulting from excessive depreciation charges. Because the Standard applies only to assets acquired after the date when the Standard must first be followed by a contractor, the impact of the Standard on recognition of gains or losses in some years in the future. At that time it is expected that guidance winl be available on the appropriate treatment for price-level changes reflected in gains or losses from disposition of fixed assets.

Current procurement regulations of Government agencies are not consistent in their provisions for gains and losses. A number of commentators were apparently unaware of this diversity; they encouraged the Board to leave the present situation alone. The existing procurement regulations have been carefully considered and the Board believes that contract cost determinations will be improved by more uniform treatment of such gains and losses.

Several commentators were concerned that the treatment of gain or loss from involuntary conversion, while in agreement with the Federal income tax treatment, differed from the generally accepted financial accounting practice. The Standard has been changed to permit the contractor to use either basis in accounting for involuntary conversions.

(11) *Original Complements*. The Standard on Capitalization of Tangible Assets defined and required the capitalization of original complements of low-cost equipment. There has been some controversy over the appropriate write-off technique for such capitalized amounts. Informal staff proposals to require amortization over the life of the complement, or of the asset for which it has been required, were challenged by contractors as being unreasonable. The Board recognized the intensity of this feeling and the June 11

proposal included a provision developed specifically to assign such costs among cost accounting periods.

Some commentators pointed out that the June 11 proposal for amortization of original complements would have required a practice which is not at all common and would be difficult to implement.

The provisions of the proposal were modified for the October 3 version to require simply that an original complement be treated as a tangible capital asset, and that the basic requirements of the Standard be applied to it. Thus, the costs of each original complement would be amortized over its period of expected usefulness, and in accordance with its pattern of expected usage, either separately or as a part of an appropriate group. Comments received on the October 3 version have suggested some misunderstanding of the principle involved. Some additional language has been added to the illustration on depreciation for original complements in § 409.60(c) to further clarify the principle that an original complement is a single asset and not a group of individual items.

(12) *Retroactive Impact of Changes.* The Board called attention, in the June 11 publication, to the conflict between some aspects of Opinion No. 20 of the Accounting Principles Board and the treatment proposed, in § 409.50(i), for changes made in depreciation accounting during the service life of an asset. The position proposed by the Board, that of making changes applicable prospectively only, was approved by most of those who commented on the point. A very few commentators asked that the Board agree with the financial accounting principle and insist upon retroactive impact, even though this would require reopening settled contracts. The Board was not convinced that any improvement in costing accuracy resulting from reopening settled contracts would merit the obvious administrative inconvenience involved. The Standard is, therefore, not changed in this regard.

(13) *Service Center Costs.* The June 11 proposal provided that when depreciable assets are part of an organizational unit whose costs are charged to users on the basis of service, the depreciation cost of such assets should be included as part of the costs of the organizational unit. A number of commentators expressed concern that the Standard might be thought to require the assignment of building depreciation separately to each organizational unit which occupied a building, even though the applicable building depreciation might be only a very minor part of the total organizational unit cost. If an organizational unit occupies a entire building, and the depreciation cost of that building is significant and can practicably be identified, that building depreciation cost should be included as a cost of the organizational unit for assignment to cost objectives on the basis of service. If, however, the total depreciation cost of a building, which is allocable to a number of cost objectives, is accounted for as indirect cost and its allocation on that basis would not materially distort the measurement of costs to any benefiting cost objective, little point would be served by insisting that each organizational unit receive a specific charge for building depreciation.

Several commentators were concerned that the paragraph on service centers might restrict the base or bases used for charging service center costs to other cost objectives. Nothing in that paragraph is intended to limit or prescribe the base or bases used for charging service center costs.

(14) *Cost of Capital.* Many commentators have pointed out that the requirements to be imposed by the Standard may result, on assets acquired after the effective date, in less depreciation charged in earlier years of asset life. The resultant slowdown in recovery of funds could, they pointed out, have an adverse impact on the profitability of defense contracts. Many of the comments seek to justify rapid write-off as a partial offset to the costs of capital actually involved but not directly recognized in contract pricing.

The purpose of this Standard is to provide a better measurement and allocation of depreciation cost. Accounting practices used for these functions should be justified on the basis of their effectiveness for such measurement and allocation. They should not be justified on the basis of problems identified with other aspects (e.g., profitability) of defense contracts.

The Board has no authority to extend itself into the area of profitability of defense contracts. This is a matter for the procuring agencies. In this regard, current procurement regulations provide guidance with respect to negotiating proposed profits; this guidance includes some implicit recognition of the cost of capital. The Board believes that accounting for the costs of capital and determining equitable measures of profit are issues separate from depreciation accounting and these issues cannot be resolved effectively by adoption of any particular depreciation practices.

(15) *Modernization and Public Policy.* Many commentators have pointed out, throughout the process of developing this Standard, that no Cost Accounting Standard should be adopted if it would interfere with public policy to encourage investment in facilities which might provide a more modern, more effective industrial mobilization base. The Board favors appropriate improvements in the physical facilities used in performance of negotiated defense contracts; its purpose however does not include such public policy decisions as the introduction or continuation of incentives to encourage investment in certain classes of assets. This Standard is being promulgated for the purpose of improving the measurement and allocation of depreciation on acquired assets. The Board does not believe that this purpose is inconsistent with or a deterrent to effective plant modernization.

(16) *Inflation Accounting.* Some commentators were concerned with the effect of inflation in depreciation accounting. They suggested that this Cost Accounting Standard should provide for the use of replacement cost or current value rather than historical cost as the basis for determining depreciable amounts. Present Government procurement regulations as well as financial and tax accounting are based on historical costs. Current inflationary trends, however, suggest that more attention should be given to the impact of inflation on established accounting concepts.

The Financial Accounting Standards Board (FASB) is considering this subject. The FASB issued an Exposure Draft on "Financial Reporting in Units of General Purchasing Power" on December 31, 1974. The CASB is also studying the subject.

The cost impact of this Standard for most contractors is some years in the future. The Standard is required to be followed by contractors at the start of their next fiscal year after receipt of a covered contract requiring compliance with this Standard. The Standard provides for a two-year period after required compliance to accumulate necessary supporting records. The requirement of the Standard for determining lives applies only to new assets acquired after the necessary records are available. Therefore, for most contractors implementation of the requirements of life determination will apply only to new assets acquired in accounting periods beginning January 1, 1978, or later.

The Board sees this Standard as establishing proper techniques for the measurement and allocation of depreciation expense. The Board believes, therefore, that this Standard can properly be promulgated at this time. The subject of inflation accounting concerns not only depreciation cost but all costs, and will be dealt with as part of the studies now in progress by both the CASB and the FASB.

(17) *Costs and Benefits.* Comments received on the June 11 and October 3 proposals indicated that there would be substantial administrative cost entailed in complying with this Standard. Part of the increased cost is attributed to required changes in accounting practices; a greater part is alleged to be related to increased controversy over the acceptability of current and proposed depreciation methods and lives.

A number of the administrative problems described in the comments have been reduced or eliminated by changes to the Standard. The requirement for recordkeeping, however, has not been eliminated. As discussed above, the Board recognizes that for some companies additional cost will be incurred to implement this aspect of the Standard. Also as discussed above, there may be some one-time analytical effort during the next two years to develop starting estimates of actual retention periods. The Board believes that these administrative costs, when reasonably managed in light of the purpose to be served, are warranted by the likelihood of better measurement of depreciation cost than has previously been available.

The Standard does not prescribe uniform accounting treatment. It enunciates principles and criteria for the implementation of these principles, which will achieve a practical degree of increased uniformity and consistency in fixed asset depreciation accounting techniques. In some cases, as for the determination of estimated service life, the Standard requires the establishment of records to achieve a better measurement of cost based on the manner in which contractors manage their fixed assets.

The benefits to be expected are better accounting for depreciation cost and enhanced ability to meet the responsibilities of the Government and of defense contractors to properly account for the expenditure of public funds. The Board recognizes that some additional costs will be incurred in obtaining compliance with this Standard. The benefits to be obtained are substantial, and the Standard contributes to fulfilling the Board's obligation to seek improved accounting for defense contracts.

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There is also being published today (40 FR 4259) an amendment to Part 400, Definitions, to incorporate in that part terms defined in § 409.30(a) of this Cost Accounting Standard.

PREAMBLE B

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 409.10. This amendment was part of a publication which added § 331.30 (b)(3). Only the portion of the preamble which describes the revision to § 409.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 410—ALLOCATION OF BUSINESS UNIT GENERAL AND ADMINISTRATIVE EXPENSES TO FINAL COST OBJECTIVES

Sec.
410.10 General applicability.
410.20 Purpose.
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APPENDIX A—TRANSITION FROM A COST OF SALES OR SALES BASE TO A COST INPUT BASE
PREAMBLES A—B

AUTHORITY: 84 Stat. 796, sec. 103, 50 U.S.C. App. 2168.

SOURCE: 41 FR 16141, Apr. 16, 1976, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble, is intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (41 FR 16141, Apr. 16, 1976) is set forth as Preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 410.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

§ 410.20 Purpose.

The purpose of this Cost Accounting Standard is to provide criteria for the allocation of business unit general and administrative (G&A) expenses to business unit final cost objectives based on their beneficial or causal relationship. These expenses represent the cost of the management and administration of the business unit as a whole. The Standard also provides criteria for the allocation of home office expenses received by a segment to the cost objectives of that segment. This Standard will increase the likelihood of achieving objectivity in the allocation of expenses to final cost objectives and comparability of cost data among contractors in similar circumstances.

§ 410.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Allocate.* To assign an item of cost or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Business unit.* Any segment of an organization, or an entire business organization which is not divided into segments.

(3) *Cost input.* The cost, except G&A expenses, which for contract costing purposes is allocable to the production of goods and services during a cost accounting period.

(4) *Cost objective.* A function, organizational subdivision, contract or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

(5) *Final cost objective.* A cost objective which has allocated to it both direct and indirect costs, and, in the contractor's accumulation systems, is one of the final accumulation points.

(6) *General and Administrative (G&A) expense.* Any management, financial, and other expense which is incurred by or allocated to a business unit and which is for the general management and administration of the business unit as a whole. G&A expense does not include those management expenses whose beneficial or causal relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

(7) *Segment.* One of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The terms includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 410.40 Fundamental requirement.

(a) Business unit G&A expenses shall be grouped in a separate indirect cost pool which shall be allocated only to final cost objectives.

(b) (1) The G&A expense pool of a business unit for a cost accounting period shall be allocated to final cost objectives of that cost accounting period by means of a cost input base representing the total activity of the business unit except as provided in paragraph (b)(2) of this section. The cost input base selected shall be the one which best represents the total activity of a typical cost accounting period.

(2) The allocation of the G&A expense pool to any particular final cost objectives which receive benefits significantly different from the benefits accruing to other final cost objectives shall be determined by special allocation. (§ 410.50(j)).

(c) Home office expenses received by a segment shall be allocated to segment cost objectives as required by § 410.50(g).

(d) Any costs which do not satisfy the definition of G&A expense but which have been classified by a business unit as G&A expenses, can remain in the G&A expense pool unless they can be allocated to business unit cost objectives on a beneficial or causal relationship which is best measured by a base other than a cost input base.

[41 FR 16141, Apr. 16, 1976, as amended at 44 FR 55127, Sept. 25, 1979]

PREAMBLE: For preamble relating to § 410.40(d), see Preamble A of the supplement to Part 420.

§ 410.50 Techniques for application.

(a) G&A expenses of a segment incurred by another segment shall be removed from the incurring segment's G&A expense pool. They shall be allocated to the segment for which the expenses were incurred on the basis of the beneficial or causal relationship between the expenses incurred and all benefiting or causing segments. If the expenses are incurred for two or more segments, they shall be allocated using an allocation base common to all such segments.

(b) The G&A expense pool may be combined with other expenses for allocation to final cost objectives provided that:

(1) The allocation base used for the combined pool is appropriate both for the allocation of the G&A expense pool under this Standard and for the allocation of the other expenses; and

(2) Provision is made to identify the components and total of the G&A expense pool separately from the other expenses in the combined pool.

(c) Expenses which are not G&A expenses and are insignificant in amount may be included in the G&A expense pool for allocation to final cost objectives.

(d) The cost input base used to allocate the G&A expense pool shall include all significant elements of that cost input which represent the total activity of the business unit. The cost input base selected to represent the total activity of a business unit during a cost accounting period may be: (1) Total cost input, (2) value-added cost input, or (3) single element cost input. The determination of which cost input base best represents the total activity of a business unit must be judged on the basis of the circumstances of each business unit.

(1) A total cost input base is generally acceptable as an appropriate measure of the total activity of a business unit.

(2) Value-added cost input shall be used as an allocation base where inclusion of material and subcontract costs would significantly distort the allocation of the G&A expense pool in relation to the benefits received, and where costs other than direct labor are significant measures of total activity. A value-added cost input base is total cost input less material and subcontract costs.

(3) A single element cost input base, e.g., direct labor hours or direct labor dollars, which represents the total activity of a business unit may be used to allocate the G&A expense pool where it produces equitable results. A single element base may not produce equitable results where other measures of activity are also significant in relation to total activity. A single element base is inappropriate where it is an insignificant part of the total cost of some of the final cost objectives.

(e) Where, prior to the effective date of this Standard, a business unit's disclosed or established cost accounting practice was to use a cost of sales or sales base, that business unit may use the transition method set out in Appendix A hereof.

(f) Cost input shall include those expenses which by operation of this Standard are excluded from the G&A expense pool and are not part of a combined pool of G&A expenses and other expenses allocated using the same allocation base.

(g) (1) Allocations of the home office expenses of (i) line management of particular segments or groups of segments, (ii) residual expenses, and (iii) directly allocated expenses related to the management and administration of the receiving segment as a whole shall be included in the receiving segment's G&A expense pool.

(2) Any separate allocation of the expenses of home office (i) centralized service functions, (ii) staff management of specific activities of segments, and (iii) central payments or accruals, which is received by a segment shall be allocated to the segment cost objectives in proportion to the beneficial or causal relationship between the cost objectives and the expense if such allocation is significant in amount. Where a beneficial or causal relationship for the expense is not identifiable with segment cost objectives, the expense may be included in the G&A expense pool.

(h) Where a segment performs home office functions and also performs as an operating segment having a responsibility for final cost objectives, the expense of the home office functions shall be segregated. These expenses shall be allocated to all benefiting or causing segments, including the segment performing the home office functions, pursuant to disclosed or established accounting practices for the allocation of home office expenses to segments.

(i) For purposes of allocating the G&A expense pool, items produced or worked on for stock or product inventory shall be accounted for as final cost objectives in accordance with the following paragraphs:

(1) Where items are produced or worked on for stock or product inventory in a given cost accounting period, the cost input to such items in that period shall be included only once in the computation of the G&A expense allocation base and in the computation of the G&A expense allocation rate for that period and shall not be included in the computation of the base or rate for any other cost accounting period.

(2) A portion of the G&A expense pool shall be allocated to items produced or worked on for stock or product inventory in the cost accounting period or periods in which such items are produced at the rates determined for such periods except as provided in paragraph (i)(3) of this section.

(3) Where the contractor does not include G&A expense in inventory as part of the cost of stock or product inventory items, the G&A rate of the cost accounting period in which such items are issued to final cost objectives may be used to determine the G&A expenses applicable to issues of stock or product inventory items.

(j) Where a particular final cost objective in relation to other final cost objectives receives significantly more or less benefit from G&A expense than would be reflected by the allocation of such expenses using a base determined pursuant to paragraph (d) of this section, the business unit shall account for this particular final cost objective by a special allocation from the G&A expense pool to the particular final cost objective commensurate with the benefits received. The amount of a special allocation to any such final cost objective shall be excluded from the G&A expense pool required by § 410.40(a), and the particular final cost objective's cost input data shall be excluded from the base used to allocate this pool.

[41 FR 16141, Apr. 16, 1976; 41 FR 22241, June 2, 1976]

§ 410.60 Illustrations.

(a) Business Unit A has been including the cost of scientific computer operations in its G&A expense pool. The scientific computer is used predominately for research and development, rather than for the management and administration of the business unit as a whole. The costs of the scientific computer operation do not satisfy the Standard's definition of G&A expense; however, they may remain in the G&A expense pool unless they can be allocated to business unit cost objectives on a beneficial or causal relationship which is best measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

(b) Segment B performs a budgeting function, the cost of which is included in its G&A expense pool. This function includes the preparation of budgets for another segment. The cost of preparing the budgets for the other segment should be removed from B's G&A expense pool and transferred to the other segment.

(c) (1) Business Unit C has a personnel function which is divided into two parts (i) a vice president of personnel who establishes personnel policy and overall guidance, and (ii) a personnel department which handles hirings, testing, evaluations, etc. The expense of the vice president is included in the G&A expense pool. The expense of the personnel department is allocated to the other indirect cost pools based on the beneficial or causal relationship between that expense and the indirect cost pools. This procedure is in compliance with the requirements of this Standard.

(2) Business Unit C has included selling costs as part of its G&A expense pool. Business Unit C wishes to continue to include selling costs in its G&A expense pool. Under the provisions of this Standard, Business Unit C may continue to include selling costs in its G&A pool, and these costs will be allocated over a cost input base selected in accordance with the provisions of § 410.50(d).

(3) Business Unit C has included IR&D and B&P costs in its G&A expense pool. C has used a cost of sales base to allocate its G&A expense pool. As of January 1, 1978 (assumed for purposes of this illustration), the date on which C must first allocate its G&A expense pool in accordance with the requirements of this Standard, C has among its final cost objectives several cost reimbursement contracts and fixed price contracts subject to the CAS clause [referred to as the pre-existing contracts]. If C chooses to use the transition method in § 410.50(e):

(i) C shall allocate IR&D and B&P costs during the transition period (from January 1, 1978, to and including the cost accounting period during which the pre-existing contracts are completed), to the pre-existing contracts as part of its G&A expense pool using a cost of sales base pursuant to § 410.50(e) and Appendix A.

(ii) During the transition period such costs, as part of the G&A expense pool, shall be allocated to new cost reimbursement contracts and new fixed price contracts subject to the CAS clause using a cost input base as required by § 410.50 (d) and (e) and Appendix A.

(iii) Beginning with the cost accounting period after the transition period the IR&D and B&P costs as part of the G&A expense pool shall be allocated to all final cost objectives using a cost input base as required by § 410.50(d). If C chooses not to use the transition method in § 410.50(e), the contractual provision requiring appropriate equitable adjustment of the prices of affected prime contracts and subcontracts will be implemented.

(4) Business Unit C has accounted for and allocated IR&D and B&P costs in a cost pool separate and apart from the G&A expense pool. C may continue to account for these costs in a separate cost pool under the provision of this Standard. If C is to use a total cost input base, these costs when accounted for and allocated in a cost pool separate and apart from the G&A expense pool will become part of the total cost input base used by C to allocate the G&A expense pool.

(5) Business Unit C has included selling costs as part of its G&A expense pool. Business Unit C has used a cost of sales base to allocate the G&A expense pool. Business Unit C desires to continue to allocate selling costs using the costs of sales base. Under the provisions of this Standard, Business Unit C would account for selling costs as a cost pool separate and apart from the G&A expense pool, and continue to allocate these costs over a cost of sales base. If C uses a total cost input base to allocate the G&A expense pool, the selling costs will become part of the total cost input base.

(d) (1) Business Unit D has accounted for selling costs in a cost pool separate and apart from its G&A expense pool and has allocated these costs using a cost of sales base. Under the provisions of this Standard, Business Unit D may continue to account for those costs in a separate pool and allocate them using a cost of sales base. Business Unit D has a total cost input base to allocate its G&A expense pool. The selling costs will become part of the cost input base used by Business Unit D to allocate the G&A expense pool.

(2) During a cost accounting period, Business Unit D buys $2,000,000 of raw materials. At the end of that cost accounting period, $500,000 of raw materials inventory have not been charged out to contracts or other cost objectives. The $500,000 of raw materials are not part of the total cost input base for the cost accounting period, because they have not been charged to the production of goods and services during that period. If all of the $2,000,000 worth of raw material had been charged to cost objectives during the cost accounting period, the cost input base for the allocation of the G&A expense pool would include the entire $2,000,000.

(3) Business Unit D manufactures a variety of testing devices. During a cost accounting period, Business Unit D acquires and uses a small building, constructs a small production facility using its own resources, and keeps for its own use one unit of a testing device that it manufactures and sells to its customers. The acquisition cost of the building is not part of the total cost input base; however, the depreciation taken on the building would be part of the total cost input base. The costs of construction of the small production facility are not part of the total cost input base. The requirements of Cost Accounting Standard 404 provide that those G&A expenses which are identifiable with the constructed asset and are material in amount shall be capitalized as part of the cost of the production facility. If there are G&A expenses material in amount and identified with the constructed asset, these G&A expenses would be removed from the G&A expense pool prior to the allocation of this pool to final cost objectives. The cost of the testing device shall be part of the total cost input base per the requirements of Cost Accounting Standard 404 which provides that the costs of constructed assets identical with the contractor's regular product shall include a full share of indirect cost.

(e) (1) Business Unit E produces Item Z for stock or product inventory. The business unit does not include G&A expense as part of the inventory cost of these items for costing or financial reporting purposes. A production run of these items occurred during Cost Accounting Period 1. A number of the units produced were not issued during Period 1 and are issued in Period 2. However, those units produced in Period 1 shall be included in the cost input of that period for calculating the G&A expense allocation base and shall not be included in the cost input of Period 2.

(2) Business Unit E should apply the G&A expense rate of Period 1 to those units of Item Z issued during Period 1 and may apply the rate of Period 2 to the units issued in Period 2.

(3) If the practice of Business Unit E is to include G&A expense as part of the cost of stock or product inventory, the inventory cost of all units of Item Z produced in Period 1 and remaining in inventory at the end of Period 1, should include G&A expense using the G&A rate of Period 1.

(f) (1) Business Unit F produced Item X for stock or product inventory. The business unit does not include G&A expense as part of the inventory cost of these items. A production run of these items was started, finished, and placed into inventory in a single cost accounting period. These items are issued during the next cost accounting period.

(2) The cost of items produced for stock or product inventory should be included in the G&A base in the same year they are produced. The cost of such items is not to be included in the G&A base on the basis of when they are issued to final cost objectives. Therefore, the time of issuance of these items from inventory to a final cost objective is irrelevant in computing the G&A base.

(g) The normal productive activity of Business Unit G includes the construction of base operating facilities for others. G uses a total cost input base to allocate G&A expense to final cost objectives. As part of a contract to construct an operating facility, G agrees to acquire a large group of trucks and other mobile equipment to equip the base operating facility. G does not usually supply such equipment. The cost of the equipment constitutes a significant part of the contract cost. A special G&A allocation to this contract shall be agreed to by the parties if they agree that in the circumstances the contract as a whole receives substantially less benefit from the G&A expense pool than that which would be represented by a cost allocation based on inclusion of the contract cost in the total cost input base.

(h) (1) The home office of Segment H separately allocates to benefiting or causing segments significant home office expenses of (i) staff management functions relative to manufacturing, (ii) staff management functions relative to engineering, (iii) central payment of health insurance costs and (iv) residual expenses. H receives these expenses as separate allocations. H maintains three indirect cost pools: (i) G&A expense, (ii) manufacturing overhead and (iii) engineering overhead; all home office expenses allocated to H are included in H's G&A expense pool.

(2) This accounting practice of H does not comply with § 410.50(g)(2). Home office residual expenses should be in the G&A expense pool, and the expenses of the staff management functions relative to manufacturing and engineering should be included in the manufacturing overhead and engineering overhead pools, respectively. The health insurance costs should be allocated in proportion to the beneficial and causal relationship between these costs and H's cost objectives.

[41 FR 16141, Apr. 16, 1976; 41 FR 22241, June 2, 1976]

§ 410.70 Exemption.

This standard shall not apply to contractors who are subject to the provisions of Federal Management Circular 74-4 (Principles for Determining Costs Applicable to Grants and Contracts with State and Local Governments).

[43 FR 24821, June 8, 1978]

PREAMBLES: For preamble to § 410.70, see preamble B of the supplement to this part. For preamble to superseded regulations see preamble A of the supplement to this part.

§ 410.80 Effective date.

(a) The effective date of this Standard is October 1, 1976.

(b) This Standard shall be followed by each contractor after the start of his next fiscal year beginning after January 1, 1977.

[41 FR 16141, Apr. 16, 1976, as amended at 41 FR 27311, July 2, 1976]

PREAMBLE: Preamble A of the supplement to Part 401 explains how effective dates are determined.

APPENDIX A—TRANSITION FROM A COST OF SALES OR SALES BASE TO A COST INPUT BASE

A business unit may use the method described below for transition from the use of a cost of sales or sales base to a cost input base.

(1) Calculate the cost of sales or sales base in accordance with the cost accounting practice disclosed or established prior to the date established by § 410.80(b) of this Cost Accounting Standard.

(2) Calculate the G&A expense allocation rate using the base determined in paragraph (1) above and use that rate to allocate from the G&A expense pool to the final cost objectives which were in existence prior to the date on which the business unit must first allocate costs in accordance with the requirements of this Cost Accounting Standard.

(3) Calculate a cost input base in compliance with § 410.50(d) above.

(4) Calculate the G&A expense rate using the base determined in paragraph (3) above and use that rate to allocate from the G&A expense pool to those final cost objectives which arise under contracts entered into on or after the date on which the business unit must first allocate costs in accordance with the requirements of this Cost Accounting Standard.

(5) The calculations set forth in paragraphs (1)-(4) above shall be performed for each cost accounting period during which final cost objectives described in (2) are being performed.

(6) The business unit shall establish an inventory suspense account. The amount of the inventory suspense account shall be equal to the beginning inventory of contracts subject to the CAS clause of the cost accounting period in which the business unit must first allocate costs in accordance with the requirements of this Cost Accounting Standard.

(7) In any cost accounting period, after the cost accounting periods described in (5) above, if the ending inventory of contracts

subject to the CAS clause is less than the balance of the inventory suspense account, the business unit shall calculate two G&A expense allocation rates, one to allocate G&A expenses to contracts subject to the CAS clause and one applicable to other work.

(a) The G&A expense pool shall be divided in the proportion which the cost input of the G&A expense allocation base of the contracts subject to the CAS clause bears to the total of the cost input allocation base, selected in accordance with § 410.50(d), for the cost accounting period.

(b) The G&A expenses applicable to contracts subject to the CAS clause shall be reduced by an amount determined by multiplying the difference between the balance of the inventory suspense account and the ending inventory of contracts subject to the CAS clause by the cost of sales rate, as determined under (1) above, of the cost accounting period in which a business unit must first allocate costs in accordance with the requirements of this Cost Accounting Standard.

(8) In any cost accounting period in which such a reduction is made, the balance of the inventory suspense account shall be reduced to be equal to the ending inventory of contracts subject to the CAS clause of that cost accounting period.

* * * * *

The following illustrates how a business unit would use this transition method.

1. Business Unit R has been using a cost of sales base to allocate its G&A expense pool to final cost objectives. Business Unit R uses a calendar year as its cost accounting period. On October 1, 1976 (assumed for purposes of this illustration) Cost Accounting Standard 410 becomes effective. On October 2, 1976, Business Unit R receives a three-year contract containing the Cost Accounting Standards clause. As a result, Business Unit R must comply with the requirements of the Standard in the cost accounting period beginning in January, 1978.

As of January 3, 1978, Business Unit R has the following contracts:

(1) Contract I—A four-year contract awarded in January, 1975.

(2) Contract II—A three-year contract which was negotiated in March, 1976, and was awarded on October 2, 1976.

(3) Contract III—A four-year contract awarded on January 2, 1978.

If Business Unit R chooses to use the transition method provided in § 410.50(e), it will allocate the G&A expense pool to these contracts as follows:

(a) Contract I—Since Contract I was in existence prior to January 1, 1978, the G&A expense pool shall be allocated to it using a cost of sales base as provided in § 410.50(e).

(b) Contract II—Since this contract was in existence prior to January 1, 1978, the G&A expense pool shall be allocated to it using a cost of sales base as provided in § 410.50(e).

(c) Contract III—Since this contract was awarded after January 1, 1978, the G&A expense pool shall be allocated to this contract using a cost input base.

Having chosen to use § 410.50(e), Business Unit R will use the transition method of allocating the G&A expense pool to final cost objectives until all contracts awarded prior to January 1, 1978, are completed (1979 if the contracts are completed on schedule). Beginning with the cost accounting period subsequent to that time, 1980, Business Unit R will use a cost input base to allocate the G&A expense pool to all cost objectives. Business Unit R will also carry forward an inventory suspense account in accordance with the requirements of this Standard.

2. A Business Unit N is first required to allocate its costs in accordance with the requirements of CAS 410 during the fiscal year beginning January 1, 1978. Business Unit N has used a cost of sales base to allocate its G&A expense pool.

During the years 1978, 1979, 1980, Business Unit N reported the following data:

	Contracts prior to Jan. 1, 1978				Contracts after Jan. 1, 1978		
	Total	Non-CAS work	CAS-fixed price work	CAS-cost contracts	Non-CAS work	CAS-fixed price work	CAS-cost contracts
Year 1978:							
Beginning inventory	$500	300	200	0	0	0	0
Cost input	+ 3000	400	600	700	500	500	300
Total	3500	700	800	700	500	500	300
Cost of sales	- 3000	600	550	700	450	400	300
Ending inventory	500	100	250	0	50	100	0
Year 1979:							
Beginning inventory	500	100	250	0	50	100	0
Cost input	+ 3000	400	600	700	500	500	300

	Contracts prior to Jan. 1, 1978				Contracts after Jan. 1, 1978		
	Total	Non-CAS work	CAS-fixed price work	CAS-cost contracts	Non-CAS work	CAS-fixed price work	CAS-cost contracts
Total	3500	500	850	700	550	600	300
Cost of sales	−2500	450	650	700	150	250	300
Ending inventory	1000	50	200	0	400	350	0
Year 1980:							
Beginning inventory	1000	50	200	0	400	350	0
Cost input	+3000	400	600	700	500	500	300
Total	4000	450	800	700	900	850	300
Cost of sales	−3250	450	800	700	450	550	300
Ending inventory	750	0	0	0	450	300	0

NOTES:
Operating data is in thousands of dollars.
G. & A. expense $375,000 in accordance with the requirements of this standard.

Work existing prior to January 1, 1978 may include:

(1) Government contracts which contain the CAS clause;

(2) Government contracts which do not contain the CAS clause;

(3) Contracts other than Government contracts or customer orders; and

(4) Production not specifically identified with contracts or customer orders under production or work orders existing prior to the date on which a business unit must first allocate its costs in compliance with this Standard and which are limited in time or quantity.

Production under standing or unlimited work orders, continuous flow processes and the like, not identified with contracts or customer orders are to be treated as final cost objectives awarded after the date on which a business unit must first allocate its costs in compliance with the requirements of this Standard.

Business Unit N may allocate the G&A expense pool as follows:

[In dollars]

	Year 1978		Year 1979		Year 1980	
1. G. & A. expense pool		375		375		375
Cost of sales rate	375/3.000 =	.125	375/2.500 =	15	375/3.250	115
Cost input rate	375/3.000 =	.125	375/3.000 =	125	375/3.000	125
2. G. & A. allocations:						
Prior contracts:						
Non-CAS work	600 × 0.125 =	75.00	450 × 0.15 =	67.50	450 × 0.115 =	51.75
CAS-fixed price work	550 × 0.125 =	68.75	650 × 0.15 =	97.50	800 × 0.115 =	92.00
CAS-cost contracts	700 × 0.125 =	87.50	700 × 0.15 =	105.00	700 × 0.115 =	80.50
After contracts:						
Non-CAS work	500 × 0.125 =	62.50	500 × 0.125 =	62.50	500 × 0.125 =	62.50
CAS-fixed price work	500 × 0.125 =	62.50	500 × 0.125 =	62.50	500 × 0.125 =	62.50
CAS-cost contracts	300 × 0.125 =	37.50	300 × 0.125 =	37.50	300 × 0.125 =	37.55
		393.75		432.50	386.70	
3. Inventory suspense account [1]		200				
G. & A. rate applicable		125				

[1] Beginning inventory of contracts subject to the CAS clause, January 1978.

2. 3 In cost accounting period 1982, Business Unit N has an ending inventory of contracts subject to the CAS clause of $100,000. This is the first cost accounting period after the transition in which the amount of the ending inventory is less than the amount of the inventory suspense account. During this cost accounting period, Business Unit N had G&A expenses of $410,000 and cost input of $3,500,000, $1,500,000 applicable to contracts subject to the CAS clause and $2,000,000 applicable to other work.

Business Unit N would compute its G&A expense allocation rate applicable to contracts subject to the CAS clause as follows:

(1) Amount of inventory suspense account	$200,000
Amount of ending inventory	100,000
Difference	100,000
G. & A. rate applicable (see A above)	×0.125
Adjustment to G. & A. expense applicable to contracts subject to the CAS clause	12,500
(2) G. & A. expense pool	410,000
G. & A. expenses applicable to contracts subject to the CAS clause ($1,500,000/ $3,500,000 × $410,000)	175,890
G. & A. expenses applicable to other work	234,110
(3) G. & A. expenses applicable to contracts subject to the CAS clause	175,890
Adjustment to G. & A. expenses applicable to contracts subject to the CAS clause	−12,500
G. & A. expenses allocable to contracts subject to the CAS clause	163,390
(4) G. & A. expense allocation rate applicable to contracts subject to the CAS clause for cost accounting period 1982—$163,390/ $1,500,000 = 0.109.	

The amount of the inventory suspense account would be reduced to $100,000.

[41 FR 16141, Apr. 16, 1976; 41 FR 22241, June 2, 1976]

PREAMBLE A

Preamble to Original Publication, 4-16-76

The following is the preamble to the original publication of Part 410, 41 FR 16141, Apr. 16, 1976, as corrected at 41 FR 22241, June 2, 1976.

The Standard on Allocation of Business Unit General and Administrative (G&A) Expenses to Final Cost Objectives being published today is one of a series being promulgated by the Cost Accounting Standards Board (CASB) pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Preliminary work on the development of this Standard was based in part on the "Report on The Feasibility of Applying Uniform Cost-Accounting Standards to Negotiated Defense Contracts," which cited the allocation of G&A expenses as one of the most frequently encountered problems in the area of allocation of indirect cost. Another basis for the early work in this area was the absence of a requirement in procurement agency regulations dealing specifically with the allocation of business unit G&A expenses. Up to now, practices related to the allocation of G&A expenses have been covered by general provisions dealing with allocability and indirect costs. These provisions do not include criteria for the selection of allocation practices in given circumstances. The Board undertook research with the view that a Cost Accounting Standard on this subject should increase the likelihood of achieving objectivity in the allocation of G&A expenses to final cost objectives and comparability of cost data among contractors in similar circumstances.

Early research included an extensive review of available literature including decisions of contract appeals boards and courts. A preliminary analysis of accounting for the allocation of G&A expenses was made and significant issues were identified. A research questionnaire based on these issues was distributed on July 28, 1972; it was designed to solicit a sample of existing practices used for the allocation of G&A expenses and the reasons supporting existing practices. Responses were obtained from 65 sources.

After evaluation of the responses to the questionnaire, the Board developed a preliminary research draft of the Standard which was widely distributed, on December 13, 1973, to obtain informal comment and to ascertain the cost impact of adoption of the Standard as proposed. The Board's further consideration of the issues related to the allocation of G&A expenses has been enhanced by almost 100 responses to this preliminary proposal.

A proposed Standard was published in the FEDERAL REGISTER of September 24, 1974, (39 FR 34300). After reviewing the responses to that publication, the Board revised its proposal. As part of its research in preparing the revised proposal, the Board surveyed, as described below, a number of companies who use a cost of sales base to allocate G&A expenses. The revised proposal was published in the FEDERAL REGISTER of September 9, 1975, (40 FR 41801). As part of the comments with the September 9, 1975 publication, the Board stated that it was particularly interested in receiving comments on the alternative methods for the proposed requirement for the transition from a cost of sales base for allocation of the G&A expense pool to use of a cost input base. Respondents were specifically asked to comment on the administrative cost and effort entailed by each of the alternatives and to indicate their preference between the alternatives. The Board supplemented both FEDERAL REGISTER publications by sending copies of the FEDERAL REGISTER material directly to organizations and individuals who had expressed an interest in the work of the Board.

The Board received a total of 136 responses to both FEDERAL REGISTER publications; 65 to the September 24, 1974 proposal and 71 to the September 9, 1975 proposal. Responses were received from individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities and others. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by organizations and individuals have resulted in a number of changes in the Standard.

The comments below summarize the issues discussed by respondents in connection with both proposed Standards. They incorporate the still relevant portions of the comments which accompanied the September 24, 1974 publication. The comments also explain the major changes which have been made to the prior proposals.

1. SELECTION OF AN ALLOCATION BASE FOR THE G&A EXPENSE POOL

Allocation Relationship. Commentators expressed the view that the choice of an allocation relationship between the G&A expense pool and final cost objectives is arbitrary; particularly, the selection of any single allocation base is arbitrary. Commentators also took the position that the G&A expense pool cannot be allocated on a demonstrable beneficial or causal relationship, that G&A is not specifically relatable to all costs, nor does it bear any relationship to cost objectives or any particular final cost objectives. Other commentators stated that the selection of the cost input base must be based on the assumption that G&A is caused by cost input. The commentators with reference to the Martin-Marietta case, ASBCA 14159, March 16, 1971, noted that the decision in that case rejected this position.

While some commentators on the September 9, 1975 publication supported the choice of cost input, others agreed with the views expressed above. The Board has concluded that the expenses in the G&A expense pool are the expenses of the general management and administration of a business unit as a whole; that the allocation base chosen should be one which measures the total activity of the business unit during a cost accounting period and not just some part of total activity, and that a cost input base accomplishes this objective.

Cost of Sales Survey. Shortly after the initial FEDERAL REGISTER publication, the Board surveyed segments of a number of companies who use a cost of sales base to allocate G&A expenses. The survey was designed to compare the results of using a cost of sales base with the results of using a cost input base to allocate these expenses. Responses were received from 91 segments. The results of the survey established that in the case of individual segments the use of a cost of sales base as compared with a cost input base can result in a significant difference in the G&A rate and in the allocations of G&A expenses to final cost objectives. For example, one of the segments in the survey had a G&A rate based on cost of sales of 8.0 percent. When that segment used a total cost input rate, its G&A rate for the same period was 10.4 percent or a 30 percent difference. A change to a total cost input rate would have resulted in substantially different allocations of G&A expense to that segment's final cost objectives.

Some commentators were critical of the Board's using a single year as the basis for the survey. These commentators noted that there could be isolated instances where the use of a cost of sales base would not produce equitable results. However, they noted that over time a cost of sales base will give equitable costing results.

For a cost of sales base to provide an equitable allocation consistent with that of an allocation to the total activity of a business unit during a cost accounting period, a contractor's mix of work between Government and commercial, types of contracts and the level of G&A expenses would have to remain constant over many periods. In this regard, the cost of sales survey demonstrated that in any given period, one period being selected, the use of a cost of sales base can result in significant differences in the allocation of G&A expenses to final cost objectives as compared with the results obtained using a cost input base.

Cost of Sales Base. A number of commentators suggested that the use of cost of sales as a measurement of the allocation base for the G&A expense pool should be permitted. Commentators asserted that this base has long been used for the allocation of the G&A expense pool and is consistent with generally accepted accounting principles and the concept of period costs. The Board's position is that the measurement of a cost of sales base is representative, in part, of the productive activities of prior periods and is subject to fluctuations which can distort the allocation of G&A expenses to activities of the current period. Although the measurement of cost of sales is based on a recorded date of sale, that is not necessarily an index of the activities of a period.

Under current regulations as interpreted by the Armed Services Board of Contract Appeals, the use of a cost of sales base will not result in an equitable allocation of G&A expenses where there are significant changes in the mix of business or significant changes in the beginning and ending inventory balances. The Board has considered the existence of these past disputes and cases involving the use of a cost of sales allocation base. In given circumstances, due to the definition and accounting for sales under various types of contracts, the cost of similar types of productive activities may be treated differently in terms of the measurement of a cost of sales allocation base. The use of a cost of sales base can result in unwarranted shifting of costs between different types of final cost objectives. Therefore, the Board has concluded that the use of a cost of sales base is inappropriate for establishing the proper cost of final cost objectives within a cost accounting period.

Cost Input Base. Commentators took the position that the use of a cost input base would violate generally accepted accounting principles used for financial accounting purposes because G&A expenses are most commonly viewed as a period cost and not allocated to production nor inventoried. The use of a cost input base would result in inventorying G&A expenses for contract costing purposes. Further, commentators asserted that there is no beneficial or causal relationship between the G&A expense pool and cost input, cost objectives or specific final cost objectives.

The logical extension of this argument is that these expenses should not be allocable to Government contracts. If no beneficial or causal relationship can be established then there should be no recovery, because for a cost to be attached to cost objectives some beneficial or causal relationship should exist.

There are a number of firms which inventory G&A expenses on Government contracts for financial disclosure purposes. Moreover, the IRS and the SEC have recognized that in some instances G&A expenses are being applied to the inventory of Government contracts, and the G&A expense pool allocation remains in the inventory of these contracts at the end of the accounting period. While the Standard does not require that G&A expense be inventoried for financial reporting purposes, the inventorying of G&A expenses on Government contracts has been an acceptable accounting procedure for financial reporting as well as for filing with the SEC. Under current IRS regulations, G&A expenses may be allocated to inventory.

The Standard being promulgated today is based on the concept of full-costing of final cost objectives. For Government contracting purposes, both direct and indirect costs, including G&A expenses, are allocable. Thus, for contract costing purposes, the concept of period expense is inapplicable. The Board has concluded that there is a beneficial or causal relationship between G&A expenses and all of the final cost objectives of a cost accounting period. Therefore, these costs are allocable to such final cost objectives.

Commentators also asserted that the Standard was unduly rigid because it permitted only one base for the allocation of the G&A expense pool. The Standard is not limited to the use of one allocation base; rather, the scope of the base, the measurement of total activity, is limited to cost input as this is the measure of the total activity of the business unit. The Standard provides that the measure of cost input best representing the total activity of the business unit during a cost accounting period is to be the one chosen as the base. The Standard includes criteria for determining the cost input base which will best measure total activity. The criteria are provided so that the allocation base for the G&A expense pool can be selected giving consideration to the differing circumstances of individual business units.

Commentators expressed a variety of views concerning the criteria for the selection of a cost input allocation base. Some commentators noted that the criteria included the necessary guidance and means for selecting the base. Others expressed concern that the criteria for selection of a particular cost input base were not clear and could lead to disputes. Some commentators expressed the view that the inclusion of value-added and single-element allocation bases was redundant. Also, a contractor should be required to demonstrate that the use of a total cost input base would not result in an appropriate allocation before the use of one of the other bases was permitted. Other commentators stated that explicit inclusion of direct labor hours and direct dollars serves to clarify the Standard. Commentators suggested that the selection criteria should be modified to remove any bias favoring a total cost input base.

The Board has recognized the merit of the numerous comments and suggestions received during the research process. The Standard has been modified to clarify the criteria for the selection of an allocation base in a particular circumstance.

Under the Standard, only a cost input base may be used. Three cost input bases have been provided and criteria have been established for selection of the appropriate base. The individual circumstances of a given business unit must be analyzed, and the cost input base that best represents the total activity of that business unit would be the base selected. The Board's research indicates that generally total cost input, because it is a broad measure of all of the work done and includes all of the costs allocable to the contracts of the period, will be a measure that is representative of the total activity of the cost accounting period.

In this context the term "total activity" refers to the production of goods and services during a cost accounting period. This scope of activity is selected in light of the fact that the purpose of this Standard is to provide guidelines for the allocation of expense to all of the work of a given cost accounting period.

Commentators questioned whether other indirect costs not part of cost of goods sold, such as unallowables and nonoperating expenses, should be part of the measurement of cost input. These commentators took the position that such costs should not be part of cost input. Commentators pointed out that there could be an inconsistency in the cost input bases used by various contractors depending on whether costs such as selling costs or IR&D and B&P costs were included in the G&A pool or excluded from the G&A pool and included as part of the cost input base. Commentators also questioned whether costs such as service center costs and intersegment transfers should be included in the cost input base for the allocation of the G&A expense pool.

The cost input base has been selected as the measure of the total activity of the work performed during the cost accounting period. Therefore, it is appropriate that the costs of all activities, functions, materials, services, etc., allocable to final cost objectives during a cost accounting period be included in the total cost input base for that period. This relationship is based on the scope of the G&A expenses which represent the cost of the general management and administration of the business unit as a whole. For example, where a total cost input base has been selected, all significant costs other than the costs included in the G&A expense pool should be included in the base. The Board is aware that there can be a difference in the allocation bases used depending upon the treatment of selling costs and IR&D and B&P costs. This result occurs from the Board's accommodation of existing practices for accounting for selling costs and IR&D and B&P costs within the structure of this Standard. The Board has specifically required the inclusion of these costs in the cost input base in § 410.50(f). The illustrations concerning the accounting for these indirect costs as part of a cost input base have been revised to clarify the required treatment.

Commentators suggested that minor variations from the specific bases presented should be allowed. The Board points out that the Standard requires that the allocation base selected should include all significant elements of cost input necessary to represent the total activity. If in a given circumstance, the exclusion of a particular item does not invalidate the chosen base's representation of total activity, this is acceptable under the Standard. The Board notes that these are the kinds of decisions which involve consideration of the individual circumstances of a business unit; accordingly, the Standard provides the opportunity for the exercise of judgment in these situations.

Commentators noted the Standard lacks an explicit consistency requirement for the use of the cost input base selected. It was pointed out that allocation bases once selected are then used for considerable periods of time, usually as long as the underlying economic circumstances do not change. In this situation the selected base would remain representative of the total activity of the business unit. The Board does not intend to change this practice. In fact, the Board notes that in concert with Cost Accounting Standard 401, the selection of the allocation base for the G&A expense pool should provide the basis for allocation of that pool until such time as the basic economic circumstances change. The Standard has been modified to require that the base selected should be one that measures activity of a typical cost accounting period.

Commentators were uncertain as to the relationship of cost input to the purchase of raw materials inventory and to Cost Accounting Standard (CAS) 404—Capitalization of Tangible Assets. To help clarify the relationship of this Standard to the purchase of raw material inventories and to CAS 404, an illustration has been added. Cost input is basically a measure of the costs and expenses allocated to production of goods and services during a cost accounting period. The illustration has been revised to make clear that items purchased for raw material inventory which have not been committed or used in production during a cost accounting period would not be part of the cost input base for that cost accounting period. As to the acquisition costs of assets constructed or fabricated by a contractor, CAS 404 and the Standard must be read together. The requirements of CAS 404 provide that those G&A expenses which are identifiable with the constructed asset and are material in amount shall be allocated to the cost of the asset. CAS 404 also provides that the cost of constructed assets that are identical with or similar to the contractor's regular product shall include a full share of indirect costs—thus, the costs of these assets will be included in the cost input base.

2. A TRANSITION PROVISION

Some commentators suggested that to avoid disputes and inequities the Board should provide a specific method of transition for any contractor that is required to change from a cost of sales or sales base to a cost input base. In the September 9, 1975 publication, the Board proposed alternative transition. Methods X and Y as a means of avoiding potential disputes and minimizing the administrative cost of implementing the change from a cost of sales or sales base to a cost input base. Either of the proposed methods would have eliminated the major portion of potential equitable adjustments arising from compliance with the Standard.

Numerous comments regarding the equity, administrative complexity, and costs of both X and Y were received. Some commentators asserted that Y was more equitable in that both CAS-covered and non-CAS covered work would be treated alike, on the basis on which the work was negotiated. Others felt X was more equitable in that there would be less impact on non-CAS covered work. Some commentators expressed the view that neither X nor Y was equitable in that both methods effectively repriced existing contracts by impacting, "squeezing down" the cost input rate on new contracts, and both methods would result in a deferral of recovery of G&A expenses.

While some commentators found one method less administratively complex than the other method, other commentators saw little difference in the administrative cost and effort required by either method. Most commentators expressed the view that either X or Y would require some additional administrative effort and the generation of data not currently produced.

A number of alternative transition methods were suggested including:

(1) An option to use either X or Y,

(2) An option to use X or Y or switch over immediately,

(3) Neither X nor Y, but use equitable price adjustment,

(4) The use of a combination method involving the actual cost of sales and cost input rates for a period and some type of suspense account to prevent an over-recovery of G&A expenses.

In addition, commentators proposed a number of variations of each of these basic alternatives. The Board is persuaded, after reviewing all of the comments received on transition methods, that a variation of one of those methods favored by many industry associations and several defense contractors offers substantial promise for avoiding potential disputes and for minimizing the impact of shifting from a cost of sales or sales base to a cost input base. This transition method is set forth in § 410.50(e) and Appendix A of the Standard. Business units required by the Standard to change from their present allocation base to a cost input base are not required to use this transition method; rather, a business unit has the option of choosing this transition method or proceeding with an immediate changeover to a cost input base and seeking adjustment under the equitable adjustment provision of the contract clause.

Use of the optional transition method will, in the Board's opinion, avoid the need to use the equitable adjustment provision of the contract clause to reprice prime contracts and subcontracts of business units using this technique. The Board believes that this procedure is appropriate for this Cost Accounting Standard.

It is the Board's view, however, that for most Standards the impact of changes in cost accounting practices required by new Cost Accounting Standards will be accommodated by price adjustments for covered prime contracts and subcontracts through the equitable adjustment provisions of the contract clause.

For any business unit which chooses not to use the transition method set forth at § 410.50(e) and Appendix A, the contractual provision requiring appropriate equitable adjustment of the prices of affected prime contracts and subcontracts will, of course, be implemented with consequent adjustment of the price of such contracts and subcontracts.

The optional transition method provided in § 410.50(e) and Appendix A permits a business unit whose disclosed or established cost accounting practice was to use a cost of sales or sales base—and which is performing work on final cost objectives which came into existence prior to the date the business unit must first allocate its cost in compliance with the requirements of this Standard—to allocate the G&A expense pool to these cost objectives using a cost of sales or sales base. These final cost objectives often include:

(1) Government contracts which contain the CAS clause;

(2) Government contracts which do not contain the CAS clause;

(3) Contracts other than Government contracts, or customer orders awarded, prior to the date the business unit must first allocate its cost in compliance with the requirements of this Standard; and

(4) Production not specifically identified with contracts or customer orders under production or work orders existing prior to the date on which a business unit must first allocate its cost in compliance with this Standard and which are limited in time or quantity.

Production under standing or unlimited work orders, continuous flow processes and the like, not identified with contracts or customer orders, are to be treated as final cost objectives awarded after the date on which a business unit must first allocate its cost in compliance with the requirements of this Standard.

The business unit will allocate its G&A expense pool to those final cost objectives which arise on or after the date on which a business unit must first allocate costs in compliance with the requirements of this Standard using a cost input base calculated in compliance with § 410.50(d).

A business unit will use the transition method until all pre-existing final cost objectives using the cost of sales or sales base are completed. At that time the business unit will be using and will continue to use a cost input base selected in accordance with the requirements of § 410.50(d) to allocate the G&A expense pool to all CAS-covered contracts.

In order to prevent possible windfalls and to provide equity to both parties to applied to the inventory suspense account must be established. The amount of the inventory suspense account shall be the beginning inventory of contracts subject to the CAS clause of the cost accounting period in which a business unit must first allocate costs in accordance with the requirements of this Standard. The G&A expense allocation rate to be applied to the inventory suspense account is the cost of sales rate for that first accounting cost period.

The suspense account will be amortized in any cost accounting period subsequent to the last cost accounting period in which final cost objectives negotiated by using a cost of sales or sales base are still being performed and in which the amount of the ending inventory of contracts subject to the CAS clause for that cost accounting period is less than the amount of the inventory suspense account. The G&A expense pool of that cost accounting period shall be reduced by the difference between the inventory suspense account and the ending inventory of contracts subject to the CAS clause of that cost accounting period times the cost of sales rate applicable to the inventory suspense account.

The Standard must be followed after the start of a contractor's next fiscal year after January 1, 1977. This long lead time provides both the Government and contractors an opportunity to prepare appropriate administrative procedures for using this transition method.

3. DEFINITION OF G&A EXPENSE

G&A Expense. Some commentators expressed the view that the definition was consistent with their current practice; others were concerned that the definition of G&A expense was narrower than those definitions currently in use, and the result might be excessive fragmentation of existing G&A expense pools to remove insignificant items.

Board research indicates that while accountants are in agreement about the general character of G&A expenses, practice has resulted in the cost of a variety of functions and expenses being included in the G&A expense pool. As a result, from the early stages of this project onward, the Board has seen a need to provide a definition of G&A expense in order to bring some uniformity to this area of accounting.

Commentators expressed concern about problems involving the classification of those persons and functions of top level management that are concerned with both the overall planning and administration of a business unit and the direction of a particular function. Some commentators suggested that top level management people could keep time records, and split their costs between the G&A expense pool and the administration of the function which they are directing. While this may be appropriate in some circumstances, the Board believes the determination of the content of the G&A expense pool and the identification and classification of expenses in a particular circumstance must be based on judgment giving consideration to the characteristics of the individual business units. Similarly, the distinction between those expenses which are other indirect costs, including manufacturing overhead and those which are G&A expenses must be based on the individual circumstances using the guidelines provided in the Standard and the definition.

The definition has been revised to provide guidance for making those decisions. The definition now requires that for an expense to be classified as G&A expense, it must be incurred for the management and administration of the business unit as a whole. Further, the definition specifically excludes from G&A expense those management expenses whose beneficial or causal relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

Commentators indicated concern and expressed some confusion regarding the interaction of the definition of G&A expense and the requirements of § 410.40(d). Commentators were uncertain as to if and when expenses which do not meet the definition of G&A expenses contained in the Standard should be removed from the G&A expense pool. The Board has revised § 410.40(d) to clearly express the Board's intent that those expenses which do not meet the definition of a G&A expense and whose beneficial or causal relationship to business unit cost objectives is best measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period should be removed from the G&A expense pool.

Materiality. With respect to the questions about materiality, the Board has several times expressed its belief that the administration of Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. See, for example, the March 1973 "Statement Of Operating Policies, Procedures and Objectives." The Board has considered the comments concerning the potential problems that could arise without a clearer statement of materiality related to the composition of the G&A expense pool. The Board believes in this instance a significance test will be particularly useful and the Standard has been appropriately modified (§ 410.50(c)).

Accounting for Specific Items of Expense in the G&A Expense Pool. Commentators also expressed concern about the treatment of specific items of expense that are sometimes found in the G&A expense pool. In particular, commentators expressed concern over the treatment of selling and marketing costs, independent research and development (IR&D) costs and bidding and proposal (B&P) costs. Commentators questioned whether under the Standard these costs were G&A expenses to be included in the G&A expense pool.

The Board recognizes that at the present time selling costs (marketing or selling costs) may constitute a significant amount of cost and are accounted for in a variety of ways. Some account for selling costs in a separate cost pool while others include selling costs as part of the G&A expense pool.

Contractors who have included selling costs in a cost pool separate and apart from the G&A expense pool may continue that practice or may change and include selling costs in their G&A expense pool. Further, contractors who will have to change the allocation base used for the G&A expense pool and who have in the past included selling costs as part of the G&A expense pool may account for selling costs by establishing a separate cost pool for the selling costs and using the allocation base they previously used for their G&A expense pool. Where selling costs are accounted for in a cost pool separate and apart from the G&A expense pool and are allocated using a different allocation base, they shall become part of the cost input base used to allocate the G&A expense pool. Also, the Board notes that the current ASPR provision related to the accounting for IR&D and B&P cost requires that generally the allocation of these costs shall be on the same basis as the contractor's allocation of his G&A expense pool, although these expenses are not termed G&A expenses. Under the provisions of this Standard, business units which have included IR&D and B&P costs in their G&A expense pool may continue to do so. Those business units which choose to use the optional transition method in § 410.50(e) and in which the IR&D and B&P costs remain in the G&A expense pool will account for these costs as follows:

(a) During the transition period, those business units which were using a cost of sales or sales base will continue to use that base to allocate the G&A expense pool to final cost objectives which were in existence as of the date the business unit must first allocate its costs in accordance with the requirements of this Cost Accounting Standard.

(b) During the transition period and subsequent to that time, the G&A expense pool would be allocated to new contracts subject to the CAS clause using a cost input base as required by § 410.50(d).

As a result of the current ASPR provision, a business unit which is required under this proposed Standard to change the allocation base used for its G&A expense pool could, because of the ASPR requirements, also be required to change the allocation base for IR&D and B&P. For those contractors who include IR&D and B&P in their G&A expense pool, this change in the business unit's method of accounting for IR&D and B&P costs, however, would be subject to the transition provision of the proposed Standard, and would only affect allocation of these costs to contracts awarded on or after the date on which a business unit must first allocate its costs in accordance with the requirements of this Standard.

Commentators expressed the view that since IR&D, B&P costs, and selling cost could become part of the allocation base for the G&A expense pool it might lead to the concept that these costs are final cost objectives themselves and should receive an individual allocation of G&A expense. As was stated in the Prefatory Comments to the September 9, 1975 publication, the Board is currently working on projects involving IR&D, B&P and selling costs. The Board at this time does not require changing the accounting for these costs. However where these expenses are treated separately and apart from the G&A expense pool they shall become part of the allocation base used to allocate the G&A expense pool to final cost objectives and are not to be treated as individual cost objectives in and of themselves.

The illustrations concerning the accounting for costs which are removed from the G&A expense pool and the accounting for IR&D and B&P costs and selling costs have been clarified in response to comments received.

Expenses Transferred from the G&A Expense Pool. Commentators expressed the view that those items which will be taken out of the G&A expense pool and transferred to the benefiting segment for which they were incurred, are not really G&A expenses of the segment but are G&A-type expenses. These expenses come out of the pool and are transferred in what might be described as a purification of the G&A expense pool before it is allocated. The Board agrees with this position, but does not believe an amendment of the Standard is necessary.

4. USE OF MEMORANDUM RECORDS

Some commentators urged that the Standard specifically permit the use of memorandum records for the allocation of G&A expenses to final cost objectives. The Board notes that even in the absence of this Standard, many contractors now use memorandum records to perform the allocation of G&A expenses for purposes of Government contracts, because in their formal records they do not make an allocation of G&A expenses to contracts or they do so on a different basis. The Board sees no need to disturb the practice of using memorandum records for the allocation of G&A expenses to final cost objectives.

5. ALLOCATION OF HOME OFFICE EXPENSES TO FINAL COST OBJECTIVES

Commentators expressed concern about the handling of home office expenses which are received by a segment as residual expenses under CAS 403 or as a lump sum which is not designated as a particular type of expense. The Standard now provides explicitly that individual handling of various types of home office expenses would be required only where a separate allocation of expenses is received from a home office, and where the amount of the allocated expense is significant.

Other commentators suggested that in given circumstances a different allocation base than the allocation base used for the allocation of home office expense to the segment may be appropriate for the allocation of home office expense to final cost objectives of the segment. The Standard does not require that the same base be used for the allocation of home office expenses to final cost objectives of the segment as was used for the allocation of home office expenses to the segment. The Standard requires establishment of a beneficial or causal relationship between the cost objectives and the expense wherever separate and significant allocations of home office expenses are received by a segment. It may be appropriate to use a different allocation base for the allocation of home office expenses received by a segment than the allocation base used to allocate home office expenses to the segment.

A number of commentators stated that allocations of home office expenses, either in total or part, are the type of expenses which should be accounted for as period expenses and should not be inventoried nor should these allocations be part of a cost input base for the allocation of the G&A expense pool as they are not part of the activity being managed. The Standard provides that certain allocations of home office expenses are always to be included in the G&A expense pool. Allocations of certain other types of home office expenses, where they are separately received and significant in amount, may or may not be included in the segment's G&A expense pool. The Standard provides that these costs shall be allocated to cost objectives of the segment based on the beneficial or causal relationship between the cost objectives and the expense. As such, where a beneficial or causal relationship between these expenses and cost objectives of the segment can be established, these expenses shall be included in cost objectives other than the segment's G&A expense pool. Where a beneficial or causal relationship for the expenses is not identifiable with other cost objectives of the segment then the expense would be included in the G&A expense pool.

The total cost of a final cost objective is made up of a variety of costs and expenses incurred in different manners and at different times. The functions and services represented by the allocation of home office expense is recognized, for contracting purposes, as part of the total cost of final cost objectives. As such, these costs are not unlike the other costs incurred in the effort to produce the final cost objectives. These costs shall become part of the appropriate cost input base selected to allocate the G&A expense pool. The illustrations have been revised to clarify that a segment must receive the home office expenses as a separate allocation if the requirements of § 410.50(g)(2) are to be applicable.

6. ALLOCATION OF G&A EXPENSES TO SPECIAL CONTRACTS

Commentators suggested that the special allocation provision be stated in terms of class of contracts or types of situations. If the G&A expense pool meets the requirements of the Standard, the existence of a need for special allocation to a class of contracts or type of situation would indicate that the allocation base being used is not representative of the total activity of the business unit during a typical cost accounting period. The Standard is designed to provide consistent accounting treatment for all contracts, except for a particular contract or other final cost objective, which is an exception to a business unit's normal operation.

The cost input allocation base for G&A expense is a broad measure which is normally representative of the total activity of a business unit during a cost accounting period. Thus, for a given final cost objective to qualify for special treatment, the difference in its beneficial or causal relationship to G&A expense as compared with the relationship of other final cost objectives to G&A expenses should be one which is apparent and capable of being supported. The provision of the Standard calls for the exercise of judgment; nonetheless, the Board believes a materiality criterion based on a measure of significantly different benefits is proper for use in evaluating and establishing a separate and exceptional allocation to a given final cost objective.

7. MISCELLANEOUS

Some commentators stated that the Standard should provide for the allocation of G&A expenses to intermediate cost objectives, such as service centers and other overhead pools. Their position was based on the concept that in various types of full-cost responsibility accounting systems, all costs are allocated to cost objectives for more accurate costing and control purposes. A few commentators stated that for certain management expenses within the G&A expense pool they are able to determine a discrete beneficial or causal relationship between these expenses and the cost objectives of the business unit. Therefore, these expenses are allocated on a separate allocation base to the cost objectives of the business unit.

Where a beneficial or causal relationship between certain management expenses and business unit cost objectives can be determined using an allocation base other than the base used for the G&A expense pool, then by definition, these management expenses are not G&A expenses and should be excluded from the G&A pool. Where a beneficial or causal relationship other than one based on a broad measure of total activity can be determined, generally the resulting allocation represents improved contract costing. However, for those expenses which are in the G&A expense pool, the Board's research indicates that the beneficial or causal relationship between these expenses and business unit activities of a cost accounting period is such that if they are allocated to intermediate cost objectives the allocation to final cost objectives could be significantly distorted.

Some commentators took the position that G&A expenses should not be allocated to stock or product inventory items. Other commentators suggested that the cost input of stock or product inventory items should be included in the G&A allocation base only in the cost accounting period when these items are used. The Board has taken the position that work on stock or product inventory items represents part of the productive activity of the business unit for a cost accounting period, and therefore, these items should receive an allocation of G&A expenses.

The Board has recognized the administrative difficulties that can arise as a result of inventorying G&A expenses on these items for contract costing purposes and at the same time complying with requirements of generally accepted accounting principles for financial reporting. The Board has concluded that a practical solution to this circumstance is provided by the accounting treatments set forth in the Standard. A contractor can include G&A expense with the inventory cost of these items for contract costing purposes and provide his own procedure for complying with generally accepted accounting principles. Alternatively, contractors who do not include G&A expenses in the inventory cost of these items in order to conform with generally accepted accounting principles, are permitted to apply G&A expenses using the G&A rate of the period in which the items are issued.

In either situation, the cost of stock or product inventory items is to be included in the computation of the allocation base in the year produced. The Board believes this procedure will provide the appropriate determination of the G&A rate for each year, and the difference in the G&A rate applicable to final cost objectives by using the G&A rate of the year in which the items are issued rather than manufactured will not be significant.

The illustration dealing with the timing of inclusion of stock or product inventory cost input in the allocation base has been revised to make clear that stock or product inventory items cost input is to be included in the year in which the cost input is incurred.

Commentators suggested that a transition provision be provided for other types of changes, e.g., changing from a value-added cost input base to a total cost input base, or removing an item of expense from the G&A expense pool, required for compliance with the Standard. The Board recognizes that a variety of changes may occur as individual business units take action necessary to comply with the Standard. The Board believes that the equitable adjustment provision of the CAS contract clause provides the best means of handling the variety of changes which may take place.

Commentators suggested that some type of exemption threshold for this Standard should be adopted. It was suggested that the threshold could be based on either total sales to the Government by a business unit or corporate entity or Government business stated as a percentage of total business. The Board is currently studying the question of whether an exemption from its regulation could be appropriately based on the proportion of total business which a contractor does with the Government. Pending the results of that study, the Board does not believe that a percentage-of-sales exemption in individual Standards is appropriate.

Cost-Benefit. Section 719(g) 50 U.S.C. App. 2168(g), as amended provides "In promulgating such standards and major rules and regulations for the implementation of such standards, the Board shall take into account, and shall report to the Congress in the transmittal required by Section 719(h)(3) hereof, the probable costs of implementation, including inflationary effects, if any, compared to the probable benefits, including advantages and improvements in the pricing, administration and settlement of contracts."

In a draft of the proposed Standard that was distributed for comment, the Board specifically requested commentators to provide data on the administrative costs of compliance with that proposal. In the second publication of the proposed Standard, the Board made the same request for data to indicate the administrative costs of compliance with Alternative X or Alternative Y. Of the 165 comments received, only two comments on the draft proposal and one comment on the second publication provided quantitative data. Many comments received indicated that there would be some administrative costs incurred in complying with this Standard. As indicated above, a number of the potential administrative problems described in the comments have been reduced or eliminated by changes to the Standard being promulgated today. Moreover, the practices of many contractors already conform with all or some of the provisions of this Standard.

Commentators indicated that part of the increased administrative cost is attributed to the transition to a cost input allocation base for those business units currently using a cost of sales allocation base. Another part of the increased administrative cost for these same business units is attributed to the accounting for the G&A expense allocated to ending inventory. The Board recognizes that these administrative costs will arise in some cases.

Among the benefits which the Board believes will be derived from use of this Standard No. 410 are a more equitable treatment of all costs incurred during a period, in terms of the G&A expense pool allocation to final cost objectives; improved measurement of the cost of final cost objectives; a reduction in disputes through the establishment of criteria for evaluation and selection of the allocation base for the G&A expense pool; increase in the likelihood of achieving objectivity in the allocation of G&A expenses to final cost objectives; and an increase in comparability of cost data, among contractors in similar circumstances.

The Board concludes that the costs anticipated for administrative compliance with this Standard when reasonably managed in light of the purposes to be served are outweighed by the probable benefits expected to be derived from its use.

As required by section 719(g) 50 U.S.C. App. 2168(g), as amended, the Board has evaluated the potential inflationary effect of this Standard. The Board has concluded that any inflationary effect of this Standard will be insignificant.

Effective Date. The availability of the transition method to contractors who choose to use it requires especial care in complying with the effective date and application provisions of the Standard. The following comments are offered to illustrate those provisions. The comments assume that the contractor has a January 1 fiscal year; contractors with different fiscal years would of course apply the requirements of the Standard using different dates appropriate to their own fiscal year. For those contractors using a cost of sales base, having a fiscal year beginning on January 1, and electing to use the transition method provided in Appendix A, all contracts entered into prior to January 1, 1978, would be accounted for using the contractor's cost of sales base in accordance with the cost accounting practice previously disclosed or established. Contracts entered on or after January 1, 1978, should be accounted for using a cost input base in accordance with the requirement of § 410.50(d). The transition period would begin January 1, 1978, and continue until all contracts entered into prior to January 1, 1978 are completed. This situation is illustrated in Appendix A, Illustration 1.

Under certain circumstances, a contractor who has been using a cost of sales base must be presumed, during the time between the effective date of this Standard and the date when it becomes applicable to him, to have elected to use the transition method provided in § 410.50(e). These circumstances arise when (1) the contractor proposes to receive an award of a contract priced by use of a cost of sales base for the entire contract and (2) the period of performance specified or anticipated for the contract extends beyond the date when the Standard becomes applicable to the contractor. Contracting agencies should take appropriate action to advise the contractor that consistent with the concepts of Part 401, Cost Accounting Standard—Consistency in Estimating, Accumulating and Reporting Costs, his decision to price the proposal entirely by use of a cost of sales base is deemed an election to operate under the transition method prescribed in § 410.50(e) when this Standard becomes applicable to him.

Those contractors using a cost of sales base, having a January 1 fiscal year, and electing to proceed with a complete change-over to a cost input base on January 1, 1978, would have to be careful to comply with Standard 401 in making proposals for those contracts which will span part or all of the period October 1, 1976, through December 31, 1977, and cost accounting periods beginning January 1, 1978, and thereafter. The proposal should indicate that the cost of sales base will be followed until the date when the requirements of this Standard must be followed; at that later time, the practice required by this Standard, a cost input base, should be proposed to be used as the contractor's practice for the remaining life of the contract.

To illustrate, assume a contractor having a January 1 fiscal year currently allocates G&A expense using a cost of sales base. When the contractor makes a proposal for a contract which will be entered into after October 1, 1976, and prior to January 1, 1978, his proposal must recognize that his G&A expense pool will be allocated by using a cost of sales base from the date of the contract through December 31, 1977, and by using a cost input base thereafter.

The Board expects that this Standard will become effective on October 1, 1976.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in § 410.30(a) of this Cost Accounting Standard.

PREAMBLE B

Preamble to document published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised § 410.70. This amendment was part of a publication which added § 331.30(b)(3). Only the portion of the preamble which describes the revision to § 410.70 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the FEDERAL REGISTER of February 16, 1977 (42 FR 9391), the Board proposed to amend section .10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

PART 411—COST ACCOUNTING STANDARD—ACCOUNTING FOR ACQUISITION COSTS OF MATERIAL

Sec.

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PREAMBLE A

AUTHORITY: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

SOURCE: 40 FR 19428, May 5, 1975, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (40 FR 19425, May 5, 1975) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 411.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

§ 411.20 Purpose.

(a) The purpose of this Cost Accounting Standard is to provide criteria for the accounting for acquisition costs of material. The Standard includes provisions on the use of inventory costing methods. Consistent application of this Standard will improve the measurement and assignment of costs to cost objectives.

(b) This Cost Accounting Standard does not cover accounting for the acquisition costs of tangible capital assets nor accountability for Government-furnished materials.

§ 411.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Allocate.* To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Business Unit.* Any segment of an organization, or an entire business organization which is not divided into segments.

(3) *Category of Material.* A particular kind of goods, comprised of identical or interchangeable units, acquired or produced by a contractor, which are intended to be sold, or consumed or used in the performance of either direct or indirect functions.

(4) *Cost Objective.* A function, organizational subdivision, contract or

other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

(5) *Material Inventory Record.* Any record used for the accumulation of actual or standard costs of a category of material recorded as an asset for subsequent cost allocation to one or more cost objectives.

(6) *Moving Average Cost.* An inventory costing method under which an average unit cost is computed after each acquisition by adding the cost of the newly acquired units to the cost of the units of inventory on hand and dividing this figure by the new total number of units.

(7) *Weighted Average Cost.* An inventory costing method under which an average unit cost is computed periodically by dividing the sum of the cost of beginning inventory plus the cost of acquisitions, by the total number of units included in these two categories.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 411.40 Fundamental requirement.

(a) The contractor shall have, and consistently apply, written statements of accounting policies and practices for accumulating the costs of material and for allocating costs of material to cost objectives.

(b) The cost of units of a category of material may be allocated directly to a cost objective provided the cost objective was specifically identified at the time of purchase or production of the units.

(c) The cost of material which (1) is used soley in performing indirect functions, or (2) is not a significant element of production cost, whether or not incorporated in an end product, may be allocated to an indirect cost pool. When significant, the cost of such indirect material not consumed in a cost accounting period shall be established as an asset at the end of the period.

(d) Except as provided in paragraphs (b) and (c) of this section, the cost of a category of material shall be accounted for in material inventory records.

(e) In allocating to cost objectives the costs of a category of material issued from company-owned material inventory, the costing method used shall be selected in accordance with the provisions of § 411.50, and shall be used in a manner which results in systematic and rational costing of issues of material to cost objectives. The same costing method shall, within the same business unit, be used for similar categories of materials.

§ 411.50 Techniques for application.

(a) Material cost shall be the acquisition cost of a category of material, whether or not a material inventory record is used. The purchase price of material shall be adjusted by extra charges incurred or discounts and credits earned. Such adjustments shall be charged or credited to the same cost objective as the purchase price of the material, except that where it is not practical to do so, the contractor's policy may provide for the consistent inclusion of such charges or credits in an appropriate indirect cost pool.

(b) One of the following inventory costing methods shall be used when issuing material from a company-owned inventory:

(1) The first-in, first-out (FIFO) method,

(2) The moving average cost method,

(3) The weighted average cost method,

(4) The standard cost method, or

(5) The last-in, first-out (LIFO) method.

(c) The method of computation used for any inventory costing method selected pursuant to the provisions of this Standard shall be consistently followed.

(d) Where the excess of the ending inventory over the beginning inventory of material of the type described in § 411.40(c) is estimated to be significant in relation to the total cost included in the indirect cost pool, the cost of such unconsumed material shall be established as an asset at the end of the period by reducing the indirect cost pool by a corresponding amount.

§ 411.60 Illustrations.

(a) Contractor "A" has one contract which requires two custom-ordered, high-value, airborne cameras. The contractor's established policy is to order such special items specifically identified to a contract as the need arises and to charge them directly to the contract. Another contract is received which requires three more of these cameras, which the contractor purchases at a unit cost which differs from the unit cost of the first two cameras ordered. When the purchase orders were placed, the contractor identified the specific contracts on which the cameras being purchased were to be used. Although these cameras are identical, the actual cost of each camera is charged to the contract for which it was acquired without establishing a material inventory record. This practice would not be a violation of this Standard.

(b) (1) A Government contract requires use of electronic tubes identified as "W." The contractor expects to receive other contracts requiring the use of tubes of the same type. In accordance with its written policy, the contractor establishes a material inventory record for electronic tube "W," and allocates the cost of units issued to the existing Government contract by the FIFO method. Such a practice would conform to the requirements of this Standard.

(2) The contractor is awarded several additional contracts which require an electronic tube which the contractor concludes is similar to the one described in paragraph (b)(1) of this section and which is identified as "Y." At the time a purchase order for these tubes is written, the contractor cannot identify the specific number of tubes to be used on each contract. Consequently, the contractor establishes an inventory record for these tubes and allocates their cost to the contracts on an average cost method. Because a FIFO method is used for a similar category of material within the same business unit, the use of an average cost method for "Y" would be a violation of this Standard.

(c) A contractor complies with the Cost Accounting Standard on standard costs (Part 407 of this chapter), and he uses a standard cost method for allocating the costs of essentially all categories of material. Also, it is the contractor's established practice to charge the cost of purchased parts which are incorporated in his end products, and which are not a significant element of production cost to an indirect cost pool. Such practices conform to this Standard.

(d) A contractor has one established inventory for type "R" transformers. The contractor allocates by the LIFO method the current costs of the individual units issued to Government contracts. Such a practice would conform to the requirements of this Standard.

(e) A contractor has established inventories for various categories of material which are used on Government contracts. During the year the contractor allocates the costs of the units of the various categories of material issued to contracts by the moving average cost method. The contractor uses the LIFO method for tax and financial reporting purposes and, at year end, applies a pooled LIFO inventory adjustment for all categories of material to Government contracts. This application of pooled costs to Government contracts would be a violation of this Standard because the lump sum adjustment to all of the various categories of material is, in effect, a noncurrent repricing of the material issues.

§ 411.70 Exemptions.

None for this Standard.

§ 411.80 Effective date.

(a) The effective date of this Standard is January 1, 1976.

(b) This Standard shall be applied to materials purchased or produced after the start of the contractor's next fiscal year beginning after receipt of a contract to which this Standard is applicable.

[40 FR 19428, May 5, 1975, as amended at 40 FR 32823, Aug. 5, 1975]

PREAMBLE: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined.

PREAMBLE A

Preamble to Original Publication, 5-5-75

The following is the preamble to the original publication of Part 411, 40 FR 19425, May 5, 1975.

The Standard on Accounting for Acquisition Costs of Material being published today is one of a series being promulgated by the Cost Accounting Standards Board (CASB) pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168) which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Preliminary work on the development of this Standard resulted from the absence of a requirement in agency regulations that the same costing method be used for similar categories of material within the same business unit and that the method be consistently applied. The Board undertook research with a view that a Cost Accounting Standard on this subject might improve cost assignment and cost measurement in accounting for acquisition costs of material.

Early research included an extensive review of available literature and a review of decisions of boards of contract appeals and courts.

A preliminary analysis of material accounting concepts was made and a number of issues were identified; comments on this analysis were obtained from interested persons. After evaluation of all of the issues, the Board developed and circulated preliminary research drafts of Standards which were widely distributed for informal comment and to ascertain the cost impact of adoption of the Standard as proposed. Suggestions and comments were received from 70 respondents; these comments were considered in developing a revised Standard which was published in the FEDERAL REGISTER of November 26, 1974, with an invitation for interested parties to submit written views and comments to the Board. The Board supplemented that FEDERAL REGISTER publication by sending copies of the FEDERAL REGISTER material directly to organizations and individuals who had provided the Board with comments on the earlier proposal or had otherwise expressed an interest in the proposal.

Responses were received from 86 sources including individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. All of these comments have been considered by the Board and those addressing areas of particular significance are discussed below, together with explanations of the changes made in the Cost Accounting Standard being promulgated from the proposal published in the FEDERAL REGISTER on November 26, 1974.

The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been received, and for the time devoted to assisting the Board in this endeavor by the many companies and individuals involved.

1. *Need for a standard.* Many comments were received questioning the need for a Standard in this area. Suggestions were received that because Disclosure Statements at present deal with this subject matter, the Board should accept them in place of a Standard. Other commentators contended that Standard 402, Consistency in Allocating Costs Incurred for the Same Purpose (4 CFR Part 402), dealt with any problems encompassed by this Standard. Some commentators argued that current practices concerning material costs used on Government contracts are well defined, of long duration, and are continually monitored by the Government. Others contended that inventory costing methods are covered by generally accepted accounting principles (GAAP) and, for this reason the Board should not issue a Standard on this subject.

With respect to the makeup of the draft Standard itself, some commentators said it was too broad, while others said it was too detailed and procedural. Some commentators stated that any Standard in this area should deal with direct materials only and should not contain any reference to indirect materials.

The Board has considered the arguments raised above as well as other facets of this particular subject matter. After studying this matter further, the Board has concluded that a Standard dealing specifically with accounting for the acquisition costs of material is needed to complement the Disclosure Statement and Cost Accounting Standard Contract Clause requirements, and to provide consistency in the application of material costing methods. Further, the Board believes that issuance of a Standard may be entirely appropriate even if the Standard does no more than establish as a Cost Accounting Standard the currently prevailing procurement regulations dealing with the allocation of costs to cost objectives. Accordingly, the Board is promulgating today a Standard, appropriately revised in light of the comments received, dealing with Accounting for Acquisition Costs of Material.

2. *Inventory costing methods.* The draft Standard published in the FEDERAL REGISTER on November 26, 1974, provided for the use of three inventory costing methods and asked commentators to identify any other methods they believed should be acceptable, for contract costing purposes, along with a justification and criteria for the use of such methods. Many commentators expressed the view that the last-in, first-out (LIFO) inventory costing method, under which the recent costs of material are allocated to cost objectives and the older costs are allocated to material remaining in inventory, should be permitted. Some commentators noted that LIFO should be allowed because it is acceptable to the Internal Revenue Service and the Securities and Exchange Commission, and because it is a recognized method for valuing inventory under generally accepted accounting principles and it is acceptable for other purposes. Other commentators expressed the view that the LIFO method results in a better matching of current costs with current revenues thereby reducing the "inventory profits" that develop during inflationary periods.

The purpose of this Standard is to provide for better allocation and measurement of material costs as they relate to specific contracts. The accounting practices used to achieve this purpose should be justified on the basis of their effectiveness for such allocation and measurement. They should not be justified solely on the basis that they are practices acceptable for tax and financial reporting purposes. Further, generally accepted accounting principles do not specify the details of cost allocations to particular contracts but are concerned with reporting the financial results of operations of the company as a whole.

The Board realizes LIFO is considered by some as a partial answer to accounting for the impact of inflation. The Board has noted, however, that most of the companies that recommended that the LIFO method be permitted for contract costing purposes charge almost all of their material to contracts at the time the material is acquired or produced. The direct allocation of the costs of materials to contracts tends to counter the effects of inflation since the current cost of the material is charged against the contract. Moreover, few of these companies use LIFO for material that is issued to contracts from inventory.

The Board believes that accounting for the impact of inflation should be the subject of a separate Standard. The Cost Accounting Standards Board is currently conducting research into this subject.

The Board did not include LIFO as a permitted inventory costing method in the draft Standard because contractors which currently follow LIFO for Government contracts use it in a manner which does not permit systematic and rational identification of the cost of material issues to specific cost objectives. The Board believes such identification is essential in cost accounting for Government contracts. Accordingly, while the Board has included the LIFO inventory costing method as a permitted method in the Standard being promulgated today, it has also included a requirement that the costing method used be applied in a manner which results in systematic and rational costing of issues of material to specific cost objectives. The costing of such issues to cost objectives must be reasonably current; it would not appear rational to hold in abeyance for months, pending a LIFO determination, the cost of materials issued to a Government contract.

3. *Direct charging of material.* The proposed Standard included a provision whereby the cost of a category of material could be allocated directly to a cost objective provided the cost objective is specifically identified on the purchase order at the time of purchase or on the work order at the time of production of material and provided there is no established material inventory account for that category of material. Some commentators felt that contractors should be permitted to allocate the cost of material directly to a contract without the identification requirement. A greater number of contractors supported the identification requirement provided by the Board. These commentators felt that if identification with the end use was feasible, direct allocation should be permitted.

Most commentators objected to the prohibition of direct allocation if a material inventory account existed. They complained that this requirement forced the contractors to stock material at their own expense. They said this requirement would discourage purchase of material in economical lots. Commentators also pointed out that this requirement would make off-site shipments uneconomical, and would adversely affect contractors' compliance with requirements in other Standards concerning their price proposals.

The Cost Accounting Standards Board favors the direct identification of costs where possible. The Board stated in its "Statement of Operating Policies, Procedures and Objectives" (March 1973):

> As an ideal, each item of cost should be assigned to the cost objective which was intended to benefit from the resource represented by the cost or, alternatively, which caused the incurrence of the cost. To approach this goal, the Board believes in the desirability of direct identification of costs with final cost objectives to the extent practical. The Board recognizes the need for care in application of the concept of direct identification of costs with final cost objectives * * *.

In furtherance of this objective, the Board has concluded that the specific identification of the end use of a category of material at the time of purchase or production should remain a requirement for the direct allocation of the cost of material. The Board is persuaded, however, that the existence of a material inventory account should not prohibit the direct allocation of the cost of material, and the Standard being promulgated has been revised to delete that prohibition. If contractors have previously established material inventory records for categories of material, however, the Standard does not require any change in this practice.

4. *Cost of material.* The draft Standard provided that material costs should be the acquisition cost of material adjusted to the extent practical by extra charges paid or discounts and credits received. Many commentators objected to this provision since they said that it is not in accordance with the practices currently followed by most companies. They argued that they charge many of the types of adjustment items referred to above to an indirect cost account and distribute those costs to all material on a base that they say is now acceptable to the Government. They also allege that there would be considerable work involved in identifying these kinds of additional charges with the individual purchases of material and to then spread the charges against the categories of material being purchased.

The Board intended this requirement to define broadly the net acquisition cost of material. This provision has been retained in the Standard being promulgated. A section has been added to the Standard stating that where it is not practical for a contractor to handle charges and credits as set out above, the contractor may provide for the consistent inclusion of such charges or credits in an appropriate indirect cost pool.

5. *Definitions.* Many comments were received on several of the definitions included in the draft Standard. Most commentators raised questions about the definitions of "Category of Material" and "Material Inventory Account."

Some commentators concluded that "Category of Material" would include items such as lubricants, paper, ink, towels, and items of that type. The

Board intended that material such as this could be handled as provided under § 411.40(c) of the promulgated Standard which permits the cost of material to be allocated, under certain conditions, to an indirect cost pool for distribution to cost objectives.

Other commentators felt that the requirement that a category of material be comprised of identical or interchangeable units would be unduly restrictive. Their contention was that different, individual items of material would have to be considered as separate categories of material. The Board intended its definition to be read in this way. It was not meant that all sheet steel, for example, should be considered as a single category of material. Most contractors would maintain separate inventory records of different sizes and thicknesses of sheet steel. Each of these would be a category of material.

Many of the comments concerning the definition of "Material Inventory Account" indicated that commentators assumed the Board was talking only about general ledger or subsidiary ledger accounts. Such is not the case. The Board was referring to any record used for accumulating the cost and quantity of material for subsequent issue to one or more cost objectives. The records the Board had in mind could include card files, computer data, bin tags, or other forms of detailed information used in the company's system of accounting for receipt and issue of material recorded as an asset.

Many commentators objected to the inclusion of the word "quantity" and the word "cost" in the definition of material inventory account. Some said they maintained records of either cost or quantity only. It was not the Board's intention that each record must show both cost and quantity. The word "quantity" has been deleted from the definition. The records referred to are those used to accumulate the cost of materials for allocation to specific cost objectives.

The Board has concluded that the definition of "Category of Material" as presented in the draft Standard published on November 26, 1974, should be retained. The reference to "Material Inventory Account" has been deleted and the term "Material Inventory Record" substituted. Several words in this definition have been changed to make it more clear that the Board is referring to any records maintained in support of general ledger or subsidiary ledger financial accounts.

6. *Need for written policies.* Many commentators said that a requirement for written policies should be deleted from this Standard. They contended that such a requirement was not in accordance with their understanding of what Cost Accounting Standards should cover. They felt the Board was becoming too deeply involved in procedural details with such a requirement.

Contractors who have submitted Disclosure Statements felt that such submission should exempt them from a requirement for written policies. They contended that in responding to the Disclosure Statement, they were, in effect, setting forth their written policies and practices.

During the Board's development of the Disclosure Statement, many contractors suggested that a Disclosure Statement such as the Board had designed was not justified because they said they had accounting manuals and similar written documents which set forth their accounting practices. They contended further that these manuals and similar written documents were available to Government auditors and provided sufficient information concerning the contractor's accounting practices. Although these manuals could not be used to fulfill the disclosure requirement, the Board recognizes that these are the kinds of documents that should contain written policies that are needed to permit effective implementation of this Standard. The Board also notes that many companies which are subject to Cost Accounting Standards are not required to file Disclosure Statements.

Some commentators questioned whether there would be a need for written policies for each category of material. Certainly the Board does not intend that this be the case. It is expected that contractors will have written policies establishing criteria which would apply to all of their material transactions.

Other commentators concluded that the written policies were listed as a requirement by the Board solely for the Government's use in determining compliance with the Standard. The Board feels that written policies and practices are beneficial as evidenced by the many companies which have them.

7. *Applicability of standard to indirect material.* The draft Standard provided a means by which a category of material used solely in performing indirect functions or which is not a significant element of production costs could be handled through an indirect cost pool rather than accumulated in a material inventory record. There was a further requirement that when quantities of such material were not consumed in a cost accounting period and were estimated to be significant in total costs, the cost of such material was to be established as an asset at the end of the period.

Many commentators stated that the Standard should not deal with indirect materials, while a few questioned the use of an indirect cost pool for allocating the cost of such material. Other commentators stated that many contractors generally do not maintain inventory records of such material and that the provision set forth in the first sentence of the preceding paragraph was necessary, otherwise the Standard might present major problems for contractors. Most of those commenting on this point recommended the retention of this provision.

Many commentators disagreed with the requirement to establish remaining material of this type as an asset at the end of the period. Some commentators felt that this requirement contradicted the first part of the provision. They argued that if the material was not a significant element of production cost and thereby was permitted to be allocated to an indirect cost pool, it did not seem logical to require that any amounts of such material should be established as an asset at the end of the period. They stated that if this situation occurred, then presumably the material should not have been charged to cost objectives through an indirect cost pool.

These commentators apparently misinterpreted the Board's intention. The draft Standard referred to the value of unconsumed material to be set up as an asset, not the amount charged to an indirect cost pool during the cost accounting period. The provision deals with significant amounts of unconsumed material of this type remaining at the end of the period.

Another commentator stated that the expensing of indirect supplies has long been a generally accepted practice and, if consistently applied, would not result in inequities in contract costing as long as unconsumed amounts do not fluctuate significantly from year to year. Other commentators were concerned that the use of the word "significant" would generate endless disputes with Government auditors since such a determination is subjective and no definition of that word was included in the Standard.

After considering all the comments the Board has received on this point, it has decided to retain the provision allowing the use of an indirect cost pool for allocation of the cost of material of the type described in this provision of the Standard. The Board is also persuaded that when quantities of such indirect material are not consumed in a cost accounting period and the excess of the ending inventory over the beginning inventory is estimated to be significant in relation to the total cost included in the indirect cost pool, the cost of such unconsumed material is to be established as an asset at the end of the period. The setting up of this material as an asset is to be accomplished by reducing the indirect cost pool by a corresponding amount.

On numerous occasions the Board has stated that it agrees that the administration of its rules, regulations, and Standards should be reasonable and not seek to deal with insignificant amounts of cost. Because of this, the Board does not believe it essential to define the term "significant" as used in this provision of the Standard. Generally accepted accounting principles, as stated in the American Institute of Certified Public Accountant's Accounting Research Bulletin No. 43, recognize that the term "inventory" includes goods to be consumed directly or indirectly in operations, such as supplies. The aforementioned requirement has therefore been retained in the Standard being promulgated.

8. *Transfers of material.* The draft Standard contained a requirement that a transfer of the cost of material from one cost objective to another was to be made at the same cost that was allocated to the initial cost objective or at the current market value. Many commentators objected to this provision on the grounds that it would be extremely difficult to identify the cost that was allocated to the initial cost objective. They contended that this requirement would also generate disagreements with Government auditors as to whether or not initial cost information was, in fact, available. Also, some commentators felt that determination of current market value would be a difficult and time consuming chore.

While not agreeing or disagreeing with the commentators' statements, the Board has concluded that the transfer of material is of sufficient significance to warrant consideration as a subject for a separate Standard. The Board has initiated a research project to consider what factors affect the cost of transfers between cost objectives and between organizations. For this reason, the provision concerning cost of transfers of material between cost objectives has been deleted from this Standard.

9. *Periodic vs. perpetual inventory accounting.* The published draft Standard contained a provision permitting either periodic or perpetual inventory accounting procedures. This was coupled with a requirement that the period for periodic inventory accounting should not be longer than one quarter of a year. It was further stated that these provisions were not intended to establish a requirement regarding the taking of physical inventories.

Many commentators stated that this provision appeared to contain contradictory statements since the periodic inventory accounting method normally requires a physical inventory when the inventory value is established. They further said that as they understand that provision, they would be required to take physical inventories quarterly, which they felt was unnecessarily frequent.

The Board was referring to the period involved for the establishment of costs of material issues, not to the taking of physical inventories. It is the Board's intention that costing of material issues should be on a current basis. To achieve this goal, the Board has inserted a requirement in the Standard that the inventory costing method used is to be applied in a manner which results in systematic and rational costing of issues of material to specific cost objectives.

10. *Costs and benefits.* Few comments were received on the subject of implementation costs of the Standard. This Standard has, for most contractors, almost no cost. It does require written policies; most contractors already have such policies. A few contractors, however, may have to establish or modify inventory policies; for these contractors there may be minimal costs.

The Board believes that this Standard will result in improved understanding of the requirements involved in accounting for acquisition costs of material during the negotiation and audit of contracts and these potential benefits will outweigh any costs of implementation.

11. *Other comments.* The published draft Standard contained a provision excepting small quantities of material used for purposes such as prototype and developmental work from the definition of an established material inventory account. While only a few commentators offered comments on this provision, in view of the revisions being made to the Standard as set out above, this provision has been deleted from the Standard.

A number of commentators raised questions concerning the potential conflict between requirements of this Standard and those set out in Standard 407, Use of Standard Costs for Direct Material and Direct Labor (4 CFR Part 407). The Board recognizes the nature of the potential conflict described by the commentators, but feels that an inventory costing method using standard costs in accordance with the requirements of Standard 407 would meet the inventory costing requirements of this Standard.

Section 411.10, *General applicability,* has been shortened and simplified from the material under this section appearing in earlier promulgated Cost Accounting Standards. The earlier material was a restatement of the statutory requirements of Pub. L. 91-379. The Board believed it was helpful to repeat this material to assist users of the Standards. However, the Board has from time to time provided for certain exemptions from the requirements to follow Cost Accounting Standards, and these exemptions were not recognized in the "applicability" sections of earlier Standards. The Board believes that the shortened material in § 411.10, referring users to the Board's detailed regulations, will provide users with helpful information on general applicability.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in § 411.30(a) of this Cost Accounting Standard.

PART 412—COST ACCOUNTING STANDARD FOR COMPOSITION AND MEASUREMENT OF PENSION COST

Sec.
412.10 General applicability.
412.20 Purpose.
412.30 Definitions.
412.40 Fundamental requirement.
412.50 Techniques for application.
412.60 Illustrations.
412.70 Exemptions.
412.80 Effective date.
Preamble A

AUTHORITY: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

SOURCE: 40 FR 43878, Sept. 24, 1975, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preambles to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. These preambles, which are intended to explain the regulations in nontechnical language, are printed in chronological order to provide an administrative history of the cost accounting standards.

The preamble to the original publication of this part (40 FR 43873, September 24, 1975) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 412.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

§ 412.20 Purpose.

The purpose of this Standard is to provide guidance for determining and measuring the components of pension cost. The Standard establishes the basis on which pension costs shall be assigned to cost accounting periods. The provisions of this Cost Accounting Standard should enhance uniformity and consistency in accounting for pension costs and thereby increase the probability that those costs are properly allocated to cost objectives.

§ 412.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meaning ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Accrued benefit cost method.* An actuarial cost method under which units of benefit are assigned to each cost accounting period and are valued as they accrue—that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date.

(This method is also known as the Unit Credit cost method.)

(2) *Actuarial assumption.* A prediction of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, pension fund earnings, changes in values of pension fund assets.

(3) *Actuarial cost method.* A technique which uses actuarial assumptions to measure the present value of future pension benefits and pension fund administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods.

(4) *Actuarial gain and loss.* The effect on pension cost resulting from differences between actuarial assumptions and actual experience.

(5) *Actuarial liability.* Pension cost attributable, under the actuarial cost method in use, to years prior to the date of a particular actuarial valuation. As of such date, the actuarial liability represents the excess of the present value of the future benefits and administrative expenses over the present value of future contributions for the normal cost for all plan participants and beneficiaries. The excess of the actuarial liability over the value of the assets of a pension plan is the Unfunded Actuarial Liability.

(6) *Defined-benefit pension plan.* A pension plan in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits.

(7) *Defined-contribution pension plan.* A pension plan in which the contributions to be made are established in advance and the benefits are determined thereby.

(8) *Funded pension cost.* The portion of pension costs for a current or prior cost accounting period that has been paid to a funding agency or, under a pay-as-you-go plan, to plan participants or beneficiaries.

(9) *Funding agency.* An organization or individual which provides facilities to receive and accumulate assets to be used either for the payment of benefits under a pension plan, or for the purchase of such benefits.

(10) *Multiemployer pension plan.* A plan to which more than one employer contributes and which is maintained pursuant to one or more collective bargaining agreements between an employee organization and more than one employer.

(11) *Normal cost.* The annual cost attributable, under the actuarial cost method in use, to years subsequent to a particular valuation date.

(12) *Pay-as-you-go cost method.* A method of recognizing pension cost only when benefits are paid to retired employees or their beneficiaries.

(13) *Pension plan.* A deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirement, provided that the benefits are paid for life or are payable for life at the option of the employees. Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees may be an integral part of a pension plan.

(14) *Projected benefit cost method.* Any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 412.40 Fundamental requirement.

(a) *Components of pension cost.* (1) For defined-benefit pension plans, the components of pension cost for a cost accounting period are (i) the normal cost of the period, (ii) a part of any unfunded actuarial liability, (iii) an interest equivalent on the unamortized portion of any unfunded actuarial liability, and (iv) an adjustment for any actuarial gains and losses.

(2) For defined-contribution pension plans, the pension cost for a cost accounting period is the net contribution required to be made for that period, after taking into account dividends and other credits, where applicable.

(b) *Measurement of pension cost.* (1) For defined-benefit pension plans, the amount of pension cost of a cost accounting period shall be determined by use of an actuarial cost method which measures separately each of the components of pension cost set forth in paragraph (a)(1) of this section, or which meets the requirements set forth in § 412.50(b)(2).

(2) Each actuarial assumption used to measure pension cost shall be separately identified and shall represent the contractor's best estimates of anticipated experience under the plan, taking into account past experience and reasonable expectations. The validity of the assumptions used may be evaluated on an aggregate, rather than on an assumption-by-assumption, basis.

(c) *Assignment of pension cost.* The amount of pension cost computed for a cost accounting period is assignable only to that period. Except for pay-as-you-go plans, the cost assignable to a period is allocable to cost objectives of that period to the extent that liquidation of the liability for such cost can be compelled or liquidation is actually effected in that period. For pay-as-you-go plans, the entire cost assignable to a period is allocable to cost objectives of that period only if the payment of benefits earned by plan participants can be compelled. If such payment is optional with the company, the amount of assignable costs allocable to cost objectives of that period is limited to the amount of benefits actually paid to retirees or beneficiaries in that period.

§ 412.50 Techniques for application.

(a) *Components of pension cost.* (1) Any portion of an unfunded actuarial liability included as a separately identified part of the pension cost of a cost accounting period shall be included in equal annual installments. Each installment shall consist of an amortized portion of the unfunded actuarial liability plus an interest equivalent on the unamortized portion of such liability. The period of amortization shall be established as follows:

(i) If amortization of an unfunded actuarial liability has begun prior to the date this Standard first becomes applicable to a contractor, no change in the amortization period is required by this Standard.

(ii) If amortization of an unfunded actuarial liability has not begun prior to the date this Standard first becomes applicable to a contractor, the amortization period shall begin with the period in which the Standard becomes applicable and shall be no more than 30 years nor less than 10 years. However, if the plan was in existence as of January 1, 1974, the amortization period shall be no more than 40 years nor less than 10 years.

(iii) Each unfunded actuarial liability resulting from the institution of new pension plans or from adoption of improvements to pension plans subsequent to the date this Standard first becomes applicable to a contractor shall be amortized over no more than 30 years nor less than 10 years.

(2) Pension costs applicable to prior years that were specifically unallowable in accordance with then existing Government contractual provisions shall be separately identified and eliminated from any unfunded actuarial liability being amortized pursuant to the provision of paragraph (a)(1) of this section, or from future normal costs if the actuarial cost method in use does not separately develop an unfunded actuarial liability. Interest earned on funded unallowable pension costs, based on the valuation rate of return, need not be included by contractors as a reduction of future years' computations of pension costs made pursuant to this Standard.

(3) A contractor shall establish and consistently follow a policy for selecting specific amortization periods for unfunded actuarial liabilities, if any, that are developed under the actuarial cost method in use. Such policy may give consideration to factors such as the size and nature of unfunded actuarial liabilities.

(4) Actuarial assumptions used in calculating the amount of an unfunded actuarial liability shall be the same as those used for other components of pension cost. If any assumptions are changed during an amortization period, the resulting increase or decrease in an unfunded actuarial liability shall be separately amortized over no more than 30 years nor less than 10 years.

(5) Actuarial gains and losses shall be identified separately from unfunded actuarial liabilities that are being amortized pursuant to the provisions of this Standard. The accounting treatment to be afforded to such gains and losses shall be consistently applied for each pension plan.

(6) An excise tax assessed pursuant to a law or regulation because of inadequate or delayed funding of a pension plan is not a component of pension cost.

(7) If any portion of the pension cost computed for a cost accounting period is not funded in that period, no amount for interest on the portion not funded in that period shall be a component of pension cost of any future cost accounting period. Conversely, if a contractor prematurely funds pension costs in a current cost accounting period, the interest earned on such premature funding, based on the valuation rate of return, may be excluded from future years' computations of pension cost made pursuant to this Standard.

(8) For purposes of this Standard, defined-benefit pension plans funded exclusively by the purchase of individual or group permanent insurance or annuity contracts shall be treated as defined-contribution pension plans. However, all other defined-benefit pension plans administered wholly or in part through insurance company contracts shall be subject to the provisions of this Standard relative to defined-benefit pension plans.

(9) If a pension plan is supplemented by a separately-funded plan which provides retirement benefits to all of the participants in the basic plan, the two plans shall be considered as a single plan for purposes of this Standard. If the effect of the combined plans is to provide defined-benefits for the plan participants, the combined plan shall be treated as a defined-benefit plan for purposes of this Standard.

(10) A multiemployer pension plan established pursuant to the terms of a collective bargaining agreement shall be considered to be a defined-contribution pension plan for purposes of this Standard.

(11) A pension plan applicable to colleges and universities that is part of a State pension plan shall be considered to be a defined-contribution pension plan for purposes of this Standard.

(b) *Measurement of pension cost.* (1) The amount of pension cost assignable to cost accounting periods shall be measured by the accrued benefit cost method or by a projected benefit cost method which identifies separately normal costs, any unfunded actuarial liability, and periodic determinations of actuarial gains and losses, except as provided in paragraph (b)(2) of this section.

(2) Any other projected benefit cost method may be used, provided that:

(i) The method is used by the contractor in measuring pension costs for financial accounting purposes;

(ii) The amount of pension cost assigned to a cost accounting period computed under such method is reduced by the excess, if any, of the value of the assets of the pension fund over the actuarial liability of the plan as determined by a projected benefit cost method set forth in paragraph (b)(1) of this section;

(iii) The contractor accumulates supplementary information identifying the actuarial gains and losses (and, separately, gains or losses resulting from changed actuarial assumptions) that have occurred since the last determination of gains and losses and the extent to which such gains and losses have been amortized through subsequent pension contributions or offset by gains and losses in subsequent cost accounting periods, and

(iv) The cost of future pension benefits is spread over the remaining average working lives of the work force.

(3) Irrespective of the projected benefit cost method used, the calculation of normal cost shall be based on a percentage of payroll for plans where the pension benefit is a function of salaries and wages and on employee service for plans where the pension benefit is not a function of salaries and wages.

(4) The cost of benefits under a pay-as-you-go pension plan shall be measured in the same manner as are the costs of defined-benefit plans whose benefits are provided through a funding agency.

(5) Actuarial assumptions should reflect long-term trends so as to avoid distortions caused by short-term fluctuations.

(6) Pension cost shall be based on provisions of existing pension plans. This shall not preclude contractors from making salary projections for plans whose benefits are based on salaries and wages, or from considering improved benefits for plans which provide that such improved benefits must be made.

(7) If the evaluation of the validity of actuarial assumptions shows that, in the aggregate, the assumptions were not reasonable, the contractor shall (i) identify the major causes for the resultant actuarial gains or losses and (ii) provide information as to the basis and rationale used for retaining or revising such assumptions for use in the ensuing cost accounting period(s).

(c) *Assignment of pension cost.* (1) Amounts funded in excess of the pension cost computed for a cost accounting period pursuant to the provisions of this Standard shall be applied to pension costs of future cost accounting periods.

(2) Evidence that the liquidation of a liability for pension cost can be compelled includes (i) provisions of law such as the funding provisions of the Employee Retirement Income Security Act of 1974, except as provided in paragraph (c)(3) of this section, (ii) a contractual agreement which requires liquidation of the liability, or (iii) the existence of rights by a third party to required liquidation of the liability.

(3) Any portion of pension cost computed for a cost accounting period that is deferred to future periods pursuant to a waiver granted under provisions of the Employee Retirement Income Security Act of 1974, shall not be assigned to the current period. Rather, such costs shall be assigned to the cost accounting period(s) in which the funding takes place.

(4) A liability for pension cost for a cost accounting period (or, for pay-as-you-go plans, for payments to retirees or beneficiaries for a period) shall be considered to be liquidated in the period if funding is effected by the date established for filing a Federal income tax return (including authorized extensions). For contractors not required to file Federal income tax returns, the date shall be that established for filing Federal corporation income tax returns.

[40 FR 43878, Sept. 24, 1975; 40 FR 4517, Oct. 2, 1975]

§ 412.60 Illustrations.

(a) *Components of pension cost.* (1) Contractor A has a defined-benefit pension plan for its employees. The contractor's policy has been to compute and fund as annual pension cost normal cost plus only interest on the unfunded actuarial liability. Pursuant to § 412.40(a)(1), the components of pension cost for a cost accounting period must now include not only the normal cost for the period and interest on the unfunded actuarial liability, but also an amortized portion of the unfunded actuarial liability. The amortization of the liability and the interest equivalent on the unamortized portion of the liability must be computed in equal annual installments.

(2) Contractor B has insured pension plans for each of two small groups of employees. One plan is funded through a group permanent insurance contract; the other plan is funded through a group deferred annuity contract. Both plans provide for defined benefits. Pursuant to § 413.50(a)(8), for purposes of this Standard the plan financed through a group permanent insurance contract shall be considered to be a defined-contribution pension plan; the net premium required to be paid for a cost accounting period (after deducting dividends and any credits) shall be the pension cost for that period. However, the group deferred annuity plan is subject to the provisions of this Standard that are applicable to defined-benefit plans.

(3) Contractor C provides pension benefits for certain hourly employees through a multiemployer defined-benefit plan. Under the collective bargaining agreement, the contractor pays six cents into the fund for each hour worked by the covered employees. Pursuant to § 412.50(a)(10), the plan shall be considered to be a defined-contribution pension plan. The payments required to be made for a cost

accounting period shall constitute the assignable pension cost for that period.

(4) Contractor D provides pension benefits for certain employees through a defined-contribution pension plan. However, the contractor has a separate fund which is used to supplement pension benefits provided for all of the participants in the basic plan in order to provide a minimum monthly retirement income to each participant. Pursuant to § 412.50(a)(9), the two plans shall be considered as a single plan for purposes of this Standard. Because the effect of the supplemental fund is to provide defined-benefits for the plan's participants, the provisions of this Standard relative to defined-benefit pension plans shall be applicable to the combined plan.

(b) *Measurement of pension cost.* (1) Contractor E has a pension plan whose costs are assigned to cost accounting periods by use of an actuarial cost method which does not separately identify actuarial gains and losses or the effect on pension cost resulting from changed actuarial assumptions. If this cost method is used to measure costs for financial accounting purposes, it may be used for purposes of this Standard, provided that the contractor developes the supplementary information set forth in § 412.50(b)(2)(iii) regarding such gains and losses and changed actuarial assumptions. In addition, the contractor must develop an actuarial liability determined by a projected benefit cost method set forth in § 412.50(b)(1). If the resultant actuarial liability is less than the value of the pension fund, the pension cost computed for the cost accounting period must be reduced by that amount (§ 412.50(b)(2)(ii)).

(2) For a number of years Contractor F has had a pay-as-you-go pension plan which provides for payments of $200 a month to employees after retirement. The contractor is currently making such payments to several retired employees and charges such payments against current income as its pension cost. For the current cost accounting period, the contractor paid benefits totaling $24,000. Contractor F's method of accounting for pension cost does not comply with the provisions of this Standard relative to pay-as-you-go plans as set forth in §§ 412.40(c) and 412.50(b)(4). The contractor should:

(i) Compute, by use of an actuarial cost method, its actuarial liability for benefits earned by plan participants. This entire liability is always unfunded for a pay-as-you-go plan.

(ii) Compute a level amount which, including an interest equivalent, would amortize the unfunded actuarial liability over a period of no less than 10 or more than 40 years.

(iii) Compute, by use of the actuarial cost method selected, a normal cost for the period.

The sum of paragraphs (b)(2)(ii) and (iii) of this section represents the amount of pension cost assignable to the period. If payment of benefits earned by plan participants can be compelled, the entire amount of cost assignable to the period is allocable to cost objectives of that period. If such payments cannot be compelled, the amount of assignable cost allocable to cost objectives of that period is limited to the amount of benefits actually paid in that period ($24,000).

(3) Contractor G has two defined-benefit pension plans which provide for fixed dollar payments to hourly employees. Under one plan, the contractor's actuary believes that the contractor will be required to increase the level of benefits by specified percentages over the next several years. In calculating pension costs, the contractor may not assume future benefits greater than that currently required by the plan. With regard to the second plan, a collective bargaining agreement negotiated with the employee's labor union provided that pension benefits will increase by specified percentages over the next several years. Because the improved benefits are required to be made, the contractor can consider such increased benefits in computing pension costs for the current cost accounting period (§ 412.50(b)(6)).

(c) *Assignment of pension cost.* Contractor H has a trusteed pension plan for its salaried employees. It computes $1 million of pension cost for a cost accounting period. Pursuant to the funding provisions of the Employee Retirement Income Security Act of 1974, the company must fund at least $800,000. Because liquidation of the liability for the portion of pension cost required by law to be funded ($800,000) can be compelled, such cost is allocable to cost objectives of the period, in accordance with § 412.40(c). If Contractor H can be compelled by the trustee or the plan participants to fund the remaining $200,000, the liability therefor is also allocable to cost objectives of that period.

§ 412.70 Exemptions.

None for this Standard.

§ 412.80 Effective date.

(a) The effective date of this Standard is January 1, 1976.

(b) This Standard shall be followed by each contractor on or after the start of his next cost accounting period beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

[40 FR 43878, Sept. 24, 1975, as amended at 40 FR 58281, Dec. 16, 1975]

PREAMBLE: Preamble A of the supplement to Part 401 of this chapter explains how effective dates are determined.

PREAMBLE A

Original Publication, 9-24-75

The following is the preamble to the original publication of Part 412, 40 FR 43873, Sept. 24, 1975.

The Cost Accounting Standard on Composition and Measurement of Pension Cost is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 715 of the Defense Production Act of 1950, as amended, Pub. L. 91-379, 50 U.S.C. app. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. This Standard establishes the components of pension cost, the bases for measuring such cost, and the criteria for assigning pension costs to cost accounting periods.

As part of the Board's early research relating to the subject of pension costs, it developed an Issues Paper in August 1973, and a preliminary draft Standard in September 1974. Both the Issues Paper and preliminary Standard were sent to a large cross-section of companies, Government agencies, industry and professional associations, actuaries, and other interested individuals. The Board received responses to these research papers which were useful in identifying the key issues involved in pension cost accounting and in developing a proposed Standard which was published in the FEDERAL REGISTER of May 5, 1975, with an invitation to interested parties to submit written views and comments to the Board. The Board also supplemented the invitation in the FEDERAL REGISTER by sending copies of the proposed Standard to several hundred organizations and individuals who had provided the Board with comments on the preliminary proposal or who had otherwise expressed interest in the subject of the Standard.

The Board received 80 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms, universities, actuaries and others in response to the FEDERAL REGISTER proposal. All of these comments have been carefully considered by the Board. The Board's views on each of the major issues discussed by commentators are outlined below, together with explanations of the changes made in the Cost Accounting Standard being promulgated.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(1) RELATIONSHIP TO THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974 AND TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

The Board received a variety of comments relative to the relationship between the proposed Standard, the Employee Retirement Income Security Act of 1974 (ERISA), and generally accepted accounting principles set forth in "Accounting for the Cost of Pension Plans," Opinion No. 8 by the Accounting Principles Board (APB-8). Some stated that, with the enactment of ERISA, Congress has expressed its will relative to pensions and a Cost Accounting Standard on pension costs which is different than ERISA is unnecessary. Others stated that APB-8 is a viable and proven document which provides sufficient guidance for both financial accounting and cost accounting purposes. Others stated that the combination of ERISA and APB-8 provides all the guidance needed for cost accounting purposes. Still others stated that a Standard should be deferred until the Federal regulations required by ERISA have been promulgated, and/or the Financial Accounting Standards Board (FASB) completes its reevaluation of APB-8.

The purpose of the Board in promulgating this Standard is to establish the accounting bases for measuring the proper amount of pension cost to be assigned to cost accounting periods for subsequent allocation to negotiated Government contracts.

ERISA establishes, among other things, minimum funding standards for pension plans and provisions affecting deductibility of pension costs for tax purposes. Although there is some commonality between the funding provisions of ERISA and the provisions of the Standard, ERISA does not provide for the measurement of pension costs for assignment among cost accounting periods or for the subsequent allocation of such costs to contracts. Accordingly, the Standard contains requirements, not contained in ERISA, to accomplish these purposes. Nevertheless, on the basis of its research, the Board is confident that the Standard being promulgated is compatible with the requirements of ERISA, i.e., compliance with the provisions of the Standard does not violate the provisions of ERISA, although certain provisions of the Standard are more restrictive than is permitted by ERISA.

APB-8 provides criteria for accounting for the cost of pension plans for financial accounting purposes. The Board believes that certain of these criteria are not appropriate for Government contract costing purposes. For example, a fundamental concept of APB-8 is that the annual pension cost to be charged to expense for financial accounting purposes is not necessarily determined by the funding of a pension plan. The Board believes that a requirement of law for annual minimum funding of pension costs on an irrevocable basis, is strong evidence that an obligation for at least such period.

The Board is aware of the FASB's projects to establish financial accounting and reporting Standards for employee benefit plans and to reevaluate APB-8, as well as the need for the cognizant Government agencies to develop regulations relative to ERISA. It is our understanding that the FASB reevaluation of APB-8 is not likely to result in a Standard that would be applicable before the end of calendar year 1976. The Board believes, however, that the issuance of a Cost Accounting Standard is needed promptly for contract costing purposes.

For example, there does not now exist any authoritative guidance which sets forth the components of pension cost that are properly includable and excludable for contract costing purposes. In addition, there are no existing criteria to resolve how the components of pension cost, once determined, shall be measured and assigned to cost accounting periods. The need for such measurement and assignment criteria for contracts is particularly critical because of the long-range projections used in computing pension cost and because the many techniques available for measuring and assigning such cost have significant impacts thereon. The significant amounts involved in annual pension cost calculations, the changes in the mix of contractors' Government and commercial business, and the settlement of individual contracts long before actual pension costs can be determined create a special need to provide criteria relative to the assignment of pension costs among cost accounting periods and the allocation of such costs to the cost objectives of the periods.

In developing the accompanying Cost Accounting Standard, the Board has attempted to stay within the general constraints of APB-8 and the funding provisions of ERISA. The Board recognizes that in the FASB's reconsideration of APB-8, the FASB could make significant changes in the manner in which pension costs are to be treated for financial accounting purposes and that the FASB's project on financial accounting and reporting for employee benefit plans may influence the conclusions reached in the reevaluation of APB-8. However, any such changes would be directed to external financial reporting and would not necessarily impact contract costing. The Board is also aware that Federal regulations which may be issued could conflict with a provision of this Standard. The Board maintains constant liaison with the FASB with regard to the two Boards' respective responsibilities for developing Standards. It also maintains liaison with the legislative and regulatory bodies responsible for developing and administering ERISA. The Board will review whatever pronouncements these bodies may issue and will make whatever revisions to the Standard it deems appropriate for contract costing purposes.

(2) NEED FOR TWO STANDARDS RELATIVE TO PENSION COST

Several commentators suggested that this Standard should deal not only with the composition and measurement of pension cost, but also with actuarial gains and losses[1] and the allocation of pension costs. The Board believes that the development of a separate Standard covering the latter two areas is advisable. First, the development of a single Standard would result in an extremely large and complex Standard that could create many problems in implementation and administration. For example, the Issues Paper developed by the Board set forth a total of 50 distinct accounting issues requiring resolution; the Standard being promulgated covers only 24 of these issues. In addition, the Board believes that the subjects covered by the two Standards are separable; a Standard can be issued relative to the composition and measurement of pension cost without creating a concurrent need for a Standard relative to the adjustment and allocation of such costs. Moreover, in computing actuarial gains and losses, it is necessary to determine how fund assets should be valued. APB-8 does not cover this aspect of pension cost accounting. In its project on accounting for pension funds, the FASB is endeavoring to specify the manner in which assets should be valued. The Board intends, as part of its continuing liaison with the FASB on this matter, to exchange research so that any possible differences in concept or approach could be minimized or eliminated entirely.

(3) TREATMENT OF ACTUARIAL GAINS AND LOSSES

The FEDERAL REGISTER proposal noted that an adjustment for actuarial gains or losses is a component of pension cost. Several commentators expressed concern over the Board's intent. Some commentators interpreted the proposed Standard as requiring that actuarial gains and losses be spread over a number of years. Other commentators believed that the proposed Standard required the immediate recognition of actuarial gains and losses.

The Board emphasizes that the Standard does not delineate how actuarial gains and losses shall be accounted for at this time. The Standard being promulgated neither requires nor prohibits immediate recognition of gains and losses or the spreading of such gains and losses to future years. Therefore, actuarial gains and losses should be accounted for in accordance with pertinent laws and regulations, and should be consistently applied. Section 412.50(a)(5) has been amended to clarify this concept.

(4) ACTUARIAL COST METHODS[2]

Many commentators expressed their concern over the section of the FEDER-

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[1] "The effect on pension cost resulting from differences between actuarial assumptions and actual experience."

[2] "A technique which uses actuarial assumptions to measure the present value of future pension benefits and pension fund

Continued

AL REGISTER proposal which limited acceptable actuarial cost methods to the accrued benefit cost method[3] or to a projected benefit cost method[4] which separately identifies unfunded actuarial liabilities[5] and actuarial gains and losses. This section, in effect, ruled out the use of an aggregate[6] cost method for measuring pension costs for negotiated Government contracts. Most of these commentators noted that ERISA and APB-8 permit these methods to be used.

The Board's primary reason for prohibiting the use of an aggregate cost method in the proposed Standard was because such a method does not disclose actuarial gains and losses. Any method that does not disclose actuarial gains and losses impairs the ability to determine whether actuarial assumptions[7] are reasonable. Actuarial assumptions are significant underlying factors for determining the amount of pension costs to be assigned among cost accounting periods. It is only when such assumptions are visible that a determination can be made that they are reasonable. The most appropriate means for determining such reasonableness is to compare assumed events with actual events.

Also, because most aggregate cost methods do not develop unfunded actuarial liabilities, the Government cannot ascertain the funding status of a plan, i.e., whether it is excessively funded at any point in time. Consequently, the Government could be making larger reimbursements than is required to defray its fair share of pension costs incurred by contractors. Many of the comments received acknowledge that most aggregate cost methods do not disclose overfunded situations.

Nevertheless, the Board is impressed by certain of the views of commentators who advocate the use of an aggregate methods. The Board recognizes that aggregate methods are widely used and that they generally spread pension costs evenly and within the periods established in the Standard for amortizing unfunded actuarial liabilities. The Board also notes that commentators stated that a required change in actuarial cost methods may result in substantial actuarial fees and, in some cases, could result in contractors violating current labor commitments.

The Board's solution to this problem was provided generally in several of the comments received. First, several commentators who recognized that an aggregate cost method does not disclose the funding status of a plan, suggested that contractors using such a cost method develop an alternative computation to determine such status. They pointed out that such a computation is required under the full funding limitation of ERISA and is often

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administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods."

[3] "An actuarial cost method under which units of benefit are assigned to each cost accounting period and are valued as they accrue—that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method.)"

[4] "Any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers."

[5] "Pension cost attributable, under the actuarial cost method in use, to years prior to the date of a particular actuarial valuation. As of such date, the actuarial liability represents the excess of the present value of the future benefits and administrative expenses over the present value of future contributions for the normal cost for all plan participants and beneficiaries. The excess of the actuarial liability over the value of the assets of a pension plan is the Unfunded Actuarial Liability."

[6] As used herein, an aggregate cost method is any actuarial cost method which spreads the entire cost of future pension benefits over the average future service lives of the current work force and which does not develop actuarial gains or losses.

[7] "A prediction of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, pension fund earnings, changes in values of pension fund assets."

required by the IRS when it believes a plan may be overfunded.

Other commentators suggested that contractors who use an aggregate cost method provide supplemental information identifying actuarial gains and losses that have occurred and the extent to which such gains and losses have been amortized through subsequent pension contributions or offset by gains and losses in subsequent accounting periods. These commentators informed us that the incremental costs of providing such additional information would be relatively minor.

Accordingly, the Board has added a section, (§ 412.50(b)(2)) which permits a contractor to use any projected benefit cost method if the contractor (1) makes an alternative computation (under a projected benefit cost method which separately discloses unfunded actuarial liabilities and actuarial gains and losses) to disclose the funding status of the plan and reduce pension cost as indicated by such computation, (2) provides supplemental information relative to actuarial gains and losses and gains or losses resulting from changed actuarial assumptions, and (3) uses that method in developing costs for financial accounting purposes.

The third requirement was added because the Board has tried unsuccessfully to ascertain criteria for determining the circumstances under which an aggregate cost method is a preferable method for assigning costs to cost accounting periods for Government contracting purposes.

Finally, to assure that the aggregate cost method used spreads pension costs within the time frames set forth in this Standard for other projected benefit cost methods, § 412.50(b)(2) requires that such aggregate cost methods spread the cost of future pension benefits over the average remaining working lives of the work force.

(5) ACTUARIAL ASSUMPTIONS

A large number of commentators were concerned with the manner in which the FEDERAL REGISTER proposal dealt with actuarial assumptions. They were particularly concerned with that provision of the proposed Standard which stated that when an actuarial assumption differs significantly from historical experience, the contractor shall provide evidence supporting its conclusion that such experience is no longer appropriate. Most commentators who objected to this provision in the Standard interpreted it as requiring separate gain and loss analyses for each assumption each time an actuarial valuation is performed. They cited the large cost of performing such analyses and noted that ERISA merely requires that actuarial assumptions be reasonable "in the aggregate."

Although the Board believes that the basis and rationale for each assumption should be made visible by contractors, it believes that the test of reasonableness of such assumptions should be applied to the end result. It is not the intent of the Board to require a separate gain or loss analysis for each assumption each time an actuarial valuation is made. Rather, the intent is that contractors not use an undocumented composite factor to represent all assumptions used in measuring pension costs, as this practice would inhibit any evaluation of the reasonableness of individual assumptions as applied to future periods. Such evaluations may be necessary when assumptions, taken in the aggregate, are found to be unreasonable, as discussed below.

Once individual actuarial assumptions have been set forth by contractors, the Board believes that the validity of these assumptions can be evaluated by the overall results obtained. Therefore, the Standard provides that the validity of the assumptions used may be evaluated in the aggregate. However, if an actuarial valuation discloses that the assumptions were not reasonable in the aggregate, the Standard requires that the contractor shall identify the major causes for the resultant actuarial gains and losses and set forth the bases and rationale used for either retaining or revising each such assumption.

In order to recognize the long-term nature of pension plans, the Standard provides in § 412.50(b)(5) that actuarial assumptions should reflect long-term trends, rather than short-term fluctuations. Also, the Standard does not specify how often determinations of actuarial gains and losses should be made. ERISA provisions require that such determinations be made not less frequently than once every three years except that more frequent determinations may be prescribed by regulation in particular cases, i.e., for plans which have sustained substantial gains or losses for several periods in succession. The Board believes that the ERISA requirements with respect to the frequency of determinations for gains and losses is equally appropriate for compliance with the provisions of the Standard at this time.

In addition to the foregoing, several commentators stated that the Standard should provide that the judgment of enrolled actuaries, as set forth in ERISA, should be determinate with respect to assumptions as well as other actuarial determinations. The Board recognizes the importance of the functions performed by enrolled actuaries with respect to actuarial determinations. However, contract terms are not imposed on actuaries; rather, it is the contractors who are parties to contracts with the Government and must bear the responsibility for compliance with the terms thereof.

(6) CALCULATIONS OF NORMAL COST[8]

The FEDERAL REGISTER proposal provided that the calculations of normal cost should be the sum of the calculations for the individual employees in the plan, except that homogeneous groupings and averages could be used if the results substantially agree with the results based on individual employee calculations. A number of commentators objected to this provision. They said that it would appear to require that two calculations be made in order to show that the use of groupings and averages gives results that agree with the results based on individual employee calculations. Some commentators stated that this requirement is unrealistic because actuaries frequently use aggregate calculations and that such aggregations can be tested against individual company or industry-wide experience. Other commentators stated that this provision would result in a single calculation for determining the assumed entry age of planned participants.

The comments received indicate that there are divergent opinions as to how normal costs shall be calculated under projected benefit cost methods. Nevertheless, the Board concludes that the methods commonly used would not materially affect the results of normal cost calculations. Accordingly, the requirement to compute normal costs on an individual basis for projected benefit cost methods has been deleted from the Standard.

The proposed Standard provided also that the calculation of normal cost shall be based on a percentage of payroll. Many commentators stated that this requirement does not recognize the fact that many pension benefits are not related to salaries. In order to accommodate these views, the Board has revised the Standard (§ 412.50(b)(3)) to provide that the calculation of normal cost shall be based on a percentage of payroll for plans where the pension benefit is a function of salaries and wages and be based on employee service for plans where the pension benefit is not related to salaries and wages.

(7) PAY-AS-YOU-GO PENSION METHODS[9]

Several commentators apparently assumed that the FEDERAL REGISTER proposal prohibited the recognition of pension costs of plans that provide benefits on a pay-as-you-go basis. One commentator stated that the Standard prohibited the recognition of the costs of pay-as-you-go plans which are not qualified for Federal income tax purposes.

The Board's view, as expressed in the FEDERAL REGISTER proposal, is not to prohibit recognizing the cost of pension benefits provided on a pay-as-you-go basis. Rather, the Board's intent is to specify how the cost of such benefits shall be measured and assigned among cost accounting periods. Moreover, the accounting treatment to be afforded to the costs of pay-as-you-go plans is not dependent on the Federal income tax status of the plan.

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[8] "The annual cost attributable, under the actuarial cost method in use, to years subsequent to a particular valuation date."

[9] "A method of recognizing pension cost only when benefits are paid to retired employees or their beneficiaries."

Accordingly, the Board has revised the provisions of the Standard relative to pay-as-you-go methods (§ 412.50(b)(4)) and has added an illustration (§ 412.60(b)(2)) to clarify its intent.

(8) UNALLOWABLE PENSION COSTS

The FEDERAL REGISTER proposal provided that the pension costs applicable to prior years that were disallowed in accordance with then-existing Government contractual provisions should be separately identified and eliminated from any unfunded actuarial liability being amortized pursuant to the provisions of the Standard. Several commentators stated that this provision is not equitable because ERISA requires that such amounts be funded.

The Board recognizes that all elements comprising an unfunded actuarial liability, including unallowable costs included therein, are required to be amortized pursuant to the funding provisions of ERISA. However, ERISA does not deal with contract costing and therefore does not deal with unallowable contract costs. The Board believes that for contract costing purposes, pension costs which were assignable to prior periods and which were specifically determined to be unallowable under then-existing contractual provisions should not be assignable to periods subsequent to the effective date of this Standard. It should be noted that the treatment of amounts funded in excess of the pension cost for a cost accounting period is separately covered in § 412.50(c)(1).

(9) AMORTIZATION OF UNFUNDED ACTUARIAL LIABILITIES

The FEDERAL REGISTER proposal included a provision requiring contractors to establish and consistently follow a policy for selecting specific amortization periods for any unfunded actuarial liabilities. The proposed Standard stated that such policy should give consideration to the size and nature of unfunded actuarial liabilities. Several commentators stated that they did not believe that the size and nature of such liabilities should govern the choice of amortization periods. The Board's intent was to permit contractors to establish different amortization periods for different types and sizes of unfunded actuarial liabilities. The Board still believes that contractors should be permitted to establish such different amortization periods. Accordingly, the Standard has been revised (§ 412.50(a)(3)) to clarify that such determinations are permissive rather than mandatory.

(10) INTEREST RESULTING FROM DELAYED FUNDING OF PENSION PLANS

The FEDERAL REGISTER proposal provided that if any portion of pension cost computed for a cost accounting period is not funded by the time established by the funding provisions of the plan, an interest equivalent on the amount not funded shall not be a component of pension cost of any other cost accounting period. Several commentators stated that this provision is inequitable because, in order for a pension plan to be viable, an amount equivalent to interest should be added to pension costs to compensate the fund for interest that would have been earned if the cost had been funded in a timely manner. Some commentators added that APB-8 requires that interest equivalents be added to pension accruals under such circumstances. Still others understood the proposed Standard to say that such interest equivalent is not a cost; they therefore disagreed with the proposed Standard.

The Board agrees that an interest equivalent should be recognized in order to determine whether the plan is properly funded. However, the Board believes that interest cost resulting from the delayed funding of a pension plan is a consequence of an investment decision and is, therefore, an investment cost rather than a component of pension cost. The interest was caused by a decision of management to use its funds for other purposes; in effect, management borrowed from the pension trust fund.

Several commentators stated that they compute pension cost at the beginning of a cost accounting period and add interest at the valuation rate to the normal cost to the date of funding. They questioned whether the

Standard would prohibit this practice. The Standard being promulgated does not prohibit this practice: *Provided*, That funding is made by the end of the cost accounting period. Accordingly, the Board has amended § 412.50(a)(7) to state that if any portion of the cost computed for a cost accounting period is not funded in that period an amount equivalent to interest computed on that portion beyond the end of that period shall not be a component of pension cost of the current or any future cost accounting period.

(11) ASSIGNMENT OF PENSION COST

Certain commentators expressed their disagreement with the sections of the FEDERAL REGISTER proposal dealing with the assignment of pension costs among cost accounting periods. The concept set forth in the proposal related in the assignment of costs to the validity of the liability for such costs. Commentators referred to the concept set forthin APB-8 that the accrual of pension expenses and the funding of pensions are not necessarily related. They stated that cost should be assigned to cost accounting periods irrespective of whether or when funded.

The Board believes that assigning pension costs to cost accounting periods on a cash basis is inappropriate from an accounting viewpoint and could lead to the improper assignment of pension costs among periods. The Board believes also that the concept which states that funding is unrelated to pension accruals is not appropriate for contract costing because, under such a concept, pension costs could be assigned to cost accounting periods and never be funded; yet such costs would be reimbursed by the Government.

The underlying concept of the Standard is that when a valid liability exists, the corresponding costs may be accrued irrespective of when the liability is liquidated. If the liability (to the pension fund or, for pay-as-you-go plans, to retirees) is not valid, it cannot be accrued; in order for it to be allocated to cost objectives of the current period, it must be liquidated (funded) in that period or within a reasonable period of time thereafter. In order to clarify its intent with regard to the allocation of pension costs to cost objectives of individual cost accounting periods, the Board has revised the wording of § 412.40(c) of the Standard.

In the FEDERAL REGISTER proposal, the Board noted that the requirement to fund a pension cost pursuant to ERISA made the liability valid and therefore made the cost assignable to the current period. Several commentators stated that ERISA permits such costs to be waived and funded over a 15-year period. They reasoned that under such circumstances it is no longer appropriate to assign such pension cost in the year for which such costs were computed. The Board believes that if the financial, position of a contractor is such that it requests and obtains such a waiver there is doubt as to validity of the liability and therefore of the cost incurred. Accordingly, it has amended the Standard to provide, in § 412.50(c)(3), that if a contractor receives such a waiver the pension costs shall be assigned to the cost accounting periods in which the funding of such cost takes place.

(12) INSURED PLANS

Several commentators stated that the section of the FEDERAL REGISTER proposal dealing with insured plans was confusing. They stated that the definition of a "separate insurance account" set forth in the proposed Standard conflicted with this section. Commentators stated that this section would seem to eliminate from the major requirements of this Standard various forms of insured plans such as deposit administration and immediate participation guarantee contracts.

The Board's intent with regard to insured plans is to treat defined-benefit plans[10] funded exclusively by the purchase of individual or group permanent insurance contracts as defined-contribution plans.[11] The Board's view relative to such plans is consistent with ERISA whose minimum funding requirements are not applicable to these plans. All other insured pension plans are subject to the provisions of this Standard. The Board has revised § 412.50(a)(8) accordingly and has eliminated the definition of separate insurance account.

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[10] "A pension plan in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits."

(13) DEFINITIONS

The Board has received a significant number of comments relative to the definitions used in the Standard. Some commentators stated that the Board should use the definitions contained in ERISA. Others stated that the Board should use the APB-8 definitions. Still others recommended that the Board should establish a single glossary of actuarial terms.

The Board recognizes that a major problem in the field of pension accounting has been the use of various terms which have the same meaning. For example, the term "prior service costs" used in APB-8, "past service costs" used in ASPR, "accrued liability" used in ERISA, and "supplemental liability" used by many actuaries have virtually the same meaning. In researching the definitions currently in use, the Board noted that one factor seemed to prevail: The glossaries in use were tailor-made for the particular documents which applied to the terms. For example, the definitions in APB-8 were written in the context of the way in which the words were intended for use in that Opinion. Similarly, the definitions used in ERISA were fashioned to be in consonance with the specific provision of the Act. The Board's primary objective in developing the definitions in this Standard is similar; the definitions should help provide a clear understanding of the concept used therein, while at the same time maintaining consistency with the thrust of the definitions used in APB-8 and ERISA.

The Board received some additional comments with regard to specific definitions set forth in the FEDERAL REGISTER proposal. One commentator expressed confusion at the terms "accrued pension liability" and "unfunded accrued pension liability" because the word "accrued" has a specific meaning in an accounting sense which is different than that intended in the Standard. The Board believes that this comment has merit and, accordingly, the Standard has been revised to use the terms "actuarial liability" and "unfunded actuarial liability."

Other commentators requested elaboration of the definition of a pension plan. Specifically, they questioned whether the definition is applicable to execute compensation plans, excess benefit plans, and other plans that may not be "qualified" for Federal income tax purposes. The Standard provides the accounting treatment for the cost of all pension plans which fall within the definition of a pension plan. Such accounting treatment is not contingent on the manner in which IRS may categorize plans for income tax purposes.

Several additional commentators questioned that portion of the definition of a pension plan which states that benefits shall be paid for life or be payable for life at the option of the employee. They questioned whether a life income settlement for an employee would fall within the meaning of this definition. The Board believes that such a settlement is, in effect, equivalent to a payment for life and thus falls within the intent of the definition.

(14) COSTS AND BENEFITS

The anticipated benefits of this Standard are improved cost measurement and increased consistency and uniformity in accounting for pension costs and assigning such costs to cost accounting periods, leading to increased assurance that the measured and assigned costs will be allocated to the proper cost objectives, including Government contracts.

When the preliminary draft Standard on pension cost was submitted to a wide cross-section of companies and individuals, the recipients were specifically asked to comment on the costs of implementing the Standard. The overwhelming majority of the respondents stated that the incremental costs of implementation should be small. In commenting on the proposed Standard published in the FEDERAL REGISTER, several respondents stated that the prohibition against use of an aggregate projected benefit cost method and the requirement to make annual gain or loss analyses of each actuarial assumption would involve additional administration costs of any significance. Since the Board has essentially eliminated these problem areas in the Standard, it believes that increased administrative costs occasioned by this Standard will be minimal. In summary, the Board believes that the benefits to be derived from this Standard clearly outweigh the costs of implementation.

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[11] "A pension plan in which the contributions to be made are established in advance and the benefits are determined thereby."

The Board expects that this Standard will become effective on January 1, 1976.

There is also being published today an Amendment to Part 400, Definitions, to incorporate in that part terms defined in § 412.30(a) of this Cost Accounting Standard.

Part 412—Cost Accounting Standard for Composition and Measurement of Pension Cost is added to read as follows:

PART 413—ADJUSTMENT AND ALLOCATION OF PENSION COST

Sec.
413.10 General applicability.
413.20 Purpose.
413.30 Definitions.
413.40 Fundamental requirement.
413.50 Techniques for application.
413.60 Illustrations.
413.70 Exemptions.
413.80 Effective date.
PREAMBLE A

AUTHORITY: 84 Stat. 796, Sec. 103, 50 U.S.C. App. 2168.

SOURCE: 42 FR 37196, July 20, 1977, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble is intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (42 FR 37196, July 20, 1977) is set forth in preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the reference following those sections.

§ 413.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (4 CFR 331.30).

§ 413.20 Purpose.

A purpose of this Standard is to provide guidance for adjusting pension cost by measuring actuarial gains and losses and assigning such gains and losses to cost accounting periods. The Standard also provides the bases on which pension cost shall be allocated to segments of an organization. The provisions of this Cost Accounting Standard should enhance uniformity and consistency in accounting for pension costs.

§ 413.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Actuarial assumption.* A prediction of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, pension fund earnings, changes in values of pension fund assets.

(2) *Actuarial cost method.* A technique which uses actuarial assumptions to measure the present value of future pension benefits and pension fund administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods.

(3) *Actuarial gain and loss.* The effect on pension cost resulting from differences between actuarial assumptions and actual experience.

(4) *Actuarial liability.* Pension cost attributable, under the actuarial cost method in use, to years prior to the date of a particular actuarial valuation. As of such date, the actuarial liability represents the excess of the present value of the future benefits and administrative expenses over the present value of future contributions for the normal cost for all plan participants and beneficiaries. The excess of the actuarial liability over the value of the assets of a pension plan is the Unfunded Actuarial Liability.

(5) *Actuarial valuation.* The determination, as of a specified date, of the normal cost, actuarial liability, value of the assets of a pension fund, and other relevant values for the pension plan.

(6) *Immediate-gain actuarial cost method.* Any of the several actuarial cost methods under which actuarial gains and losses are included as part of the unfunded actuarial liability of the pension plan, rather than as part of the normal cost of the plan.

(7) *Normal cost.* The annual cost attributable, under the actuarial cost method in use, to years subsequent to a particular valuation date.

(8) *Pension plan.* A deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirement, provided that the benefits are paid for life or are payable for life at the option of the employees. Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees may be an integral part of a pension plan.

(9) *Pension plan participant.* Any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit from a pension plan which covers employees of such employer or members of such organization who have satisfied the plan's participation requirements, or whose beneficiaries are receiving or may be eligible to receive any such benefit. A participant whose employment status with the employer has not been terminated is an active participant of the employer's pension plan.

(10) *Projected benefit cost method.* Any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers.

(11) *Segment.* One of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(12) *Spread-gain actuarial cost method.* Any of the several projected benefit actuarial cost methods under which actuarial gains and losses are included as part of the current and future normal costs of the pension plan.

(13) *Termination gain or loss.* An actuarial gain or loss resulting from the difference between the assumed and actual rates at which plan participants separate from employment for reasons other than retirement, disability, or death.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 413.40 Fundamental requirement.

(a) *Assignment of actuarial gains and losses.* Actuarial gains and losses shall be calculated annually and shall be asssigned to the cost accounting period for which the actuarial valuation is made and subsequent periods.

(b) *Valuation of the assets of a pension fund.* The value of all pension fund assets shall be determined under an asset valuation method which takes into account unrealized appreciation and depreciation of pension fund assets, and shall be used in measuring the components of pension cost.

(c) *Allocation of pension cost to segments.* Contractors shall allocate pension cost to each segment having participants in a pension plan. A separate calculation of pension cost for a segment is required when the conditions set forth in § 413.50(c) (2) and (3) are present. When these conditions are not present, allocations may be made by calculating a composite pension cost for two or more segments and allocating this cost to these segments by means of an allocation base.

§ 413.50 Techniques for application.

(a) *Assignment of actuarial gains and losses.* (1) In accordance with the provisions of 4 CFR Part 412, actuarial gains and losses shall be identified separately from unfunded actuarial liabilities being amortized.

(2) Actuarial gains and losses determined under a pension plan whose costs are measured by an immediate-gain actuarial cost method shall be amortized over a 15-year period in equal annual installments, beginning with the date as of which the actuarial valuation is made. The installment for a cost accounting period shall consist of an element for amortization of the gain or less and an element for interest on the unamortized balance at the beginning of the period. If the actuarial gain or loss determined for a cost accounting period is not material, the entire gain or loss may be included as a component of the current or ensuing year's pension cost.

(3) Actuarial gains and losses applicable to a pension plan whose costs are measured by a spread-gain actuarial cost method shall be included as part of current and future normal cost and spread over the remaining average working lives of the work force.

(b) *Valuation of the assets of a pension fund.* (1) The actuarial value of the assets of a pension fund shall be used (i) in measuring actuarial gains and losses, and (ii) for purposes of measuring other components of pension cost.

(2) The actuarial value of the assets of a pension fund may be determined by the use of any recognized asset valuation method which provides equivalent recognition of appreciation and depreciation of pension fund assets. However, the total asset value produced by the method used shall fall within a corridor from 80 to 120 percent of the market value of the assets, determined as of the valuation date. If the method produces a value that falls outside the corridor, the value of the assets shall be adjusted to equal the nearest boundary of the corridor.

(3) The method selected for valuing pension fund assets shall be consistently applied from year to year within each plan.

(4) The provisions of paragraphs (b) (1) through (3) of this section are not applicable to plans that are funded with insurance companies under contracts where the insurance company guarantees benefit payments.

(c) *Allocation of pension cost to segments.* (1) For contractors who compute a composite pension cost covering plan participants in two or more segments, the base to be used for allocating such costs shall be representative of the factors which the pension benefits are based. For example, a base consisting of salaries and wages shall be used for pension costs that are calculated as a percentage of salaries and wages; a base consisting of the number of employees shall be used for pension costs that are calculated as an amount per employee.

(2) Separate pension cost for a segment shall be calculated whenever any of the following conditions exist for that segment, provided that such condition(s) materially affect the amount of pension cost allocated to the segment:

(i) There is a material termination gain or loss attributable to the segment,

(ii) The level of benefits, eligibility for benefits, or age distribution is materially different for the segment than for the average of all segments, or

(iii) The appropriate assumptions relating to termination, retirement age, or salary scale are, in the aggregate, materially different for the segment than for the average of all segments. Calculations of termination gains or losses shall give consideration to factors such as unexpected early retirements, benefits becoming fully vested, and reinstatements or transfers without loss of benefits. An amount may be estimated for future reemployments.

(3) Pension cost shall also be separately calculated for a segment under circumstances where—

(i) The pension plan for that segment becomes merged with that of another segment, and

(ii) The ratios of assets to actuarial liabilities for each of the merged plans are materially different from one another after applying the benefits in effect after the merger.

(4) Whenever the pension cost of a segment is required to be calculated separately pursuant to paragraphs (c) (2) and (3) of this section, such calculations shall be prospective only; pension costs need not be redetermined for prior years.

(5) For a segment whose pension costs are required to be calculated separately pursuant to paragraph (c)(2) of this section, there shall be an initial allocation of a share in the undivided pension fund assets to that segment, as follows:

(i) If the necessary data are readily determinable, the amount of assets to be allocated to the segment shall be the amount of funds contributed by, or on behalf of, the segment, increased by income received on such funds, and decreased by benefits and expenses paid from such funds; (ii) if the data specified in paragraph (i) of this paragraph (c)(5), are not readily determinable the actuarial value of the pension fund's assets shall be allocated to the segment in a manner consistent with the actuarial cost method or methods used to compute pension cost. For a segment whose pension costs are required to be calculated separately pursuant to paragraph (c)(3) of this section the initial allocation of assets to the segment shall be the market value of the segment's assets as of the date of the merger.

(6) If prior to the time a contractor is required to use this Standard, it has been calculating pension cost separately for individual segments, the amount of assets previously allocated to those segments need not be changed.

(7) After the initial allocation of assets, the contractor shall maintain a record of the portion of subsequent contributions, income, benefit payments, and expenses attributable to the segment and paid from the pension fund; income and expenses shall include a portion of any investment gains and losses attributable to the assets of the pension fund. Fund income and expenses shall be allocated to the segment in the same proportion that the assets allocated to the segment bears to total fund assets as of the beginning of the period for which fund income and expenses are being allocated.

(8) If plan participants transfer among segments, contractors need not transfer assets or liabilities unless a transfer is sufficiently large to distort the segments' ratio of fund assets to actuarial liabilities.

(9) Contractors who separately calculate the pension cost of one or more segments may calculate such cost either for all pension plan participants assignable to the segment(s) or for only the active participants of the segment(s). If costs are calculated only for active participants, a separate segment shall be created for all of the inactive participants of the pension plan and the cost thereof shall be calculated. When a contractor makes such an election, assets shall be allocated to the segment for inactive participants in accordance with paragraphs (c) (5), (6), and (7) of this section. When an employee of a segment becomes inactive, assets shall be transferred from that segment to the segment established to accumulate the assets and actuarial liabilities for the inactive plan participants. The amount of funds transferred shall be that portion of the actuarial liabilities for these inactive participants that have been funded. If inactive participants become active, funds and liabilities shall similarly be transferred to the segments to which the participants are assigned. Such transfers need be made only as of the last day of a cost accounting period. The total annual pension cost for a segment having active lives shall be the amount calculated for the segment plus an allocated portion of the pension cost calculated for

the inactive participants. Such an allocation shall be on the same basis as that set forth in paragraph (c)(1) of this section.

(10) Where pension cost is separately calculated for one or more segments, the acturaial cost method used for a plan shall be the same for all segments, as required by 4 CFR 412.50(b). Unless a separate calculation of pension cost for a segment is made because of a condition set forth in paragraph (c)(2)(iii) of this section, the same actuarial assumptions may be used for all segments covered by a plan.

(11) If a pension plan has participants in the home office of a company, the home office shall be treated as a segment for purposes of allocating the cost of the pension plan. Pension cost allocated to a home office shall be a part of the costs to be allocated in accordance with the appropriate requirements of 4 CFR Part 403.

(12) If a segment is closed, the contractor shall determine the difference between the actuarial liability for the segment and the market value of the assets allocated to the segment, irrespective of whether or not the pension plan is terminated. The determination of the actuarial liability shall give consideration to any requirements imposed by agencies of the United States Government. In computing the market value of assets for the segment, if the contractor has not already allocated assets to the segment, such an allocation shall be made in accordance with the requirements of paragraph (c)(5) (i) and (ii) of this section. The market value of the assets allocated to the segment shall be the segment's proportionate share of the total market value of the assets of the pension fund. The calculation of the difference between the market value of the assets and the actuarial liability shall be made as of the date of the event (e.g., contract termination) that caused the closing of the segment. If such a date cannot be readily determined, or if its use can result in an inequitable calculation, the contracting parties shall agree on an appropriate date. The difference between the market value of the assets and the actuarial liability for the segment represents an adjustment of previously-determined pension costs.

§ 413.60 Illustrations.

(a) *Assignment of actuarial gains and losses.* Contractor A has a defined-benefit pension plan whose costs are measured under an immediate-gain actuarial cost method. The contractor makes actuarial valuations every other year. In the past, at each valuation date, the contractor has calculated the actuarial gains and losses that have occurred since the previous valuation date and has merged such gains and losses with the unfunded actuarial liabilities that are being amortized. Pursuant to § 413.40(a), the contractor must make an actuarial valuation annually. Any actuarial gains or losses measured must be separately amortized over a 15-year period beginning with the period for which the actuarial valuation is made (§ 413.50(a) (1) and (2)).

(b) *Valuation of the assets of a pension fund.* Contractor B has a defined benefit pension plan, the assets of which are invested in equity securities, debt securities, and real property. The contractor, whose cost accounting period is the calendar year, has an annual actuarial valuation of the pension fund in June of each year; the effective date of the valuation is the beginning of that year. The contractor's method for valuing the assets of the pension fund is as follows: debt securities expected to be held to maturity are valued on an amortized basis running from initial cost at purchase to par value at maturity; land and buildings are valued at cost less depreciation taken to date; all equity securities and debt securities not expected to be held to maturity are valued on the basis of a 5-year moving average of market values. In making an actuarial valuation, the contractor must compare the values reached under the asset valuation method used with the market values of all of the assets (§ 413.40(b)). In this case, the assets are valued as of January 1 of that year. The contractor established the following values as of the valuation date.

	Asset valuation method	Market
Cash	$100,000	$100,000
Equity securities	6,000,000	7,800,000
Debt securities expected to be held to maturity	550,000	600,000
Other debt securities	600,000	750,000
Land and buildings, net of depreciation	400,000	750,000
Total	$7,650,000	$10,000,000

Section 413.50(b)(2) requires that the total value of the assets of the pension fund fall within a corridor from 80 to 120 percent of market. The corridor for the plan's assets as of January 1 is from $12 million to $8 million. Because the asset value reached by the contractor—$7,650,000—falls outside the corridor, the value reached must be adjusted to equal the nearest boundary of the corridor: $8 million. In subsequent years the contractor must continue to use the same method for valuing assets (§ 413.50(b)(3)). If the value produced falls inside the corridor, such value shall be used in measuring pension cost.

(c) *Allocation of pension cost to segments.* (1) Contractor C has a defined-benefit pension plan covering employees at five segments. Pension cost is computed by use of an immediate-gain actuarial cost method. One segment (X) is devoted primarily to performing work for the Government. During the current cost accounting period, Segment X had a large and unforeseeable reduction of employees because of a contract termination at the convenience of the Government and because the contractor did not receive an anticipated follow-on contract to one that was completed during the period. As a result, the plan has a large net termination gain. As a consequence of this gain a separate calculation of the pension cost for Segment X would result in a materially different allocation of costs to that segment than would a composite calculation and allocation by means of a base. Accordingly, pursuant to § 413.50(c)(2), the contractor must calculate a separate pension cost for Segment X. In doing so, the entire termination gain must be assigned to Segment X and amortized over 15 years. If the actuarial assumptions for Segment X continue to be substantially the same as for the other segments, the termination gain may be separately amortized and allocated only to Segment X; all other Segment X computations may be included as part of the composite calculation. After the gain is amortized, the contractor is no longer required to separately calculate the costs for Segment X unless subsequent events require such separate calculation.

(2) Contractor D has a defined-benefit pension plan covering employees at ten segments, all of which have some contracts subject to Cost Accounting Standards. The contractor uses a spread-gain actuarial cost method and calculates pension cost by developing a pension cost rate and applying that rate to the salaries and wages of the work force. One of the segments (Segment Y) is entirely devoted to Government work. The contractor's policy is to place junior employees in this segment. The age distribution of the employees of the segment is so different from that of the other segments that the pension cost for Segment Y would be materially different if computed separately than if computed as part of a computation which averages the ages of all employees covered by the plan. Pursuant to § 413.50(c)(2), the contractor must compute the pension cost for Segment Y as if it were a separate pension plan. Accordingly, the contractor must allocate a portion of the pension fund's assets to Segment Y. Memorandum records may be used in making the allocation. However, because this portion cannot be readily determined, § 413.50(c)(5)(ii) permits the allocation to be made on the basis of the actuarial cost method or methods used to calculate prior years' pension cost for the plan. Once the assets have been allocated, in future cost accounting periods the contractor shall make separate pension cost calculations for Segment Y based on the actual age distribution for the segment. Because the factors comprising pension cost for the other nine segments are relatively equal, the contractor may compute pension cost for these nine segments by using composite factors and developing a percentage of payroll for the nine segments.

The pension cost allocated to each of the nine segments shall be the product of the percentages developed and the payroll of each segment (§ 413.50 (c)(1)).

(3) Contractor E has a defined-benefit pension plan which covers employees at 12 segments. The contractor uses composite actuarial assumptions to develop a pension cost for all segments. Three of these segments primarily perform Government work; the work at the other nine segments is primarily commercial. Employee turnover at the segments performing commercial work is relatively stable. However, employment experience at the Government segments has been very volatile; there have been large fluctuations in employment levels and the contractor assumes that this pattern of employment will continue to occur. It is evident that separate termination assumptions for the Government segments and the commercial segments will result in materially different pension costs for the Government segments. Therefore, the cost for these segments must be separately calculated, using the appropriate termination assumptions for these segments (§ 413.50(c)(2)(iii)).

(4) Contractor F has a defined-benefit pension plan covering employees at 25 segments. Twelve of these segments primarily perform Government work; the remaining segments perform primarily commercial work. The contractor's records show that the termination experience and projections for the 12 segments are so different from that of the average of all of the segments that separate pension cost calculations are required for these segments pursuant to § 413.50(c)(2). However, because the termination experience and projections are about the same for all 12 segments, contractor F may calculate a composite pension cost for the 12 segments and allocate the cost to these segments by use of an appropriate allocation base.

(5) After this Standard becomes applicabale to Contractor G, it acquires Contractor H and makes it Segment H. Prior to the merger, each contractor had its own defined-benefit pension plan. Under the terms of the merger, Contractor H's pension plan and plan assets were merged with those of Contractor G. The actuarial assumptions, current salary scale, and other plan characteristics and about the same for Segment H and Contractor G's other segments. However, based on the same benefits at the time of the merger, the plan of Contractor H had a disproportionately larger unfunded actuarial liability than did Contractor G's plan. Any combining of the assets and actuarial liabilities of both plans would result in materially different pension cost allocation to Contractor G's segments than if pension cost were computed for Segment H on the basis that it had a separate pension plan. Accordingly, pursuant to § 413.50(c)(5), Contractor G must allocate to Segment H a portion of the assets of the combined plan. The amount to be allocated shall be the market value of Segment H's pension plan assets at the date of the merger, adjusted for subsequent receipts and expenditures applicable to the segment (§ 413.50(c)(7)). Contractor G must use these amounts of assets as a basis for calculating the annual pension cost applicable to Segment H.

(6) Contractor I has a defined-benefit pension plan covering employees at seven segments. The contractor has been making a composite pension cost calculation for all of the segments. However, the contractor determines that, pursuant to this Standard, separate pension costs must be calculated for one of the segments. In accordance with § 413.50(c)(9), the contractor elects to allocate fund assets only for the active participants of that segment. The contractor must then create a segment to accumulate the assets and actuarial liabilities for the plan's inactive participants. When active participants of a segment become inactive, the contractor must transfer assets to the segment for inactive participants to cover the actuarial liabilities for the participants that become inactive. However, the amount to be transferred shall be proportionate to the percentage of such liabilities that are funded.

(7) Contractor J has a defined-benefit pension plan covering employees at ten segments. The contractor makes a composite pension cost calculation for

all segments. The contractor's records show that the termination experience for one segment—primarily performing Government work—has been significantly different from the average turnover experience of the other segments. Moreover, the contractor assumes that such different experience will continue. Because of this fact, and because the application of a different termination assumption would result in significantly different costs being charged to the Government, the contractor must develop separate pension cost for that segment. In accordance with § 413.50(c)(2), the amount of pension cost must be based on an acceptable termination assumption for that segment; however, as provided in § 413.50(c)(10), all other assumptions for that segment may be the same as those for the remaining segments.

(8) Contractor K has a five-year contract to operate a Government-owned facility. The employees of that facility are covered by the contractor's overall defined-benefit pension plan which covers salaried and hourly employees at other locations. At the conclusion of the five-year period, the Government decides not to renew the contract. Although some employees are hired by the successor contractor, as far as Contractor K is concerned, the facility is closed. Pursuant to § 413.50(c)(12), Contractor K must compute an unfunded actuarial liability for the pension plan for that facility. The contractor first calculates the actuarial liability as of the date the contract expired. Because many of Contractor K's employees are terminated from the pension plan, the Internal Revenue Service considers it to be a partial plan termination, and thus requires that the terminated employees become fully vested in their accrued benefits to the extent such benefits are funded. Taking this factor into consideration, the actuary calculates the actuarial liability as amounting to $12.5 million. The contractor must then determine the market value of the pension fund assets allocable to the facility, pursuant to § 413.50(c)(5), as of the date agreed to by the contracting parties (§ 413.50(c)(12))—the date the contract expired. In making this determination the contractor establishes the ratio of the actuarial value of the assets allocable to the segment to the total actuarial value of the assets of the pension fund. The product of this ratio and the market value of all pension fund assets is the market value of the assets allocated to the segment. In this case, the market value of the segment's assets amounted to $13.8 million. Thus, for this facility the value of pension fund assets exceeded the actuarial liability by $1.3 million. This amount indicates the extent to which the Government overcontributed to the pension plan for the segment and, accordingly, indicates the extent to which prior years' pension costs are subject to adjustment.

§ 413.70 Exemptions.

None for this Standard.

§ 413.80 Effective date.

(a) The effective date of this Standard is March 10, 1978.

(b) This Standard shall be followed by each contractor on or after the start of his next cost accounting period beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

PREAMBLE A

Preamble to Original Publication, 6-2-76

The following is the preamble to the orginal publication of Part 413, 42 FR 37191, July 20, 1977.

The cost Accounting Standard on Adjustment and Allocation of Pension Cost is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub. L. 91-379, 50 U.S.C. app. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

This Standard is the second Standard dealing with pension costs. The first Standard, 4 CFR Part 412, establishes requirements covering the composition of pension cost and the bases to be used for measuring such cost. The Standard being promulgated today establishes the basis for assigning actuarial gains and losses to cost accounting periods and for allocating pension cost to segments of an organization.

As part of the Board's early research relating to the subject of pension cost, it submitted an issues paper to a large cross-section of companies, Government agencies, industry and professional associations, actuaries, and other interested individuals. On June 18, 1976, this staff draft Standard was sent to those interested parties who had expressed a desire to assist the Board in its research efforts. The responses to the staff draft Standard were considered in developing a proposed Standard which was published in the FEDERAL REGISTER of February 3, 1977, with an invitation to readers to submit written views and comments to the Board. The Board also supplemented the invitation in the FEDERAL REGISTER by sending copies of the proposed Standard to over 1,000 organizations and individuals.

The Board received 67 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms, actuaries, universities, and others in response to the FEDERAL REGISTER proposal. All of these comments have been carefully considered by the Board. The Board's views on each of the major issues discussed by commentators are outlined below, together with explanations of the changes made to the proposed Cost Accounting Standard.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(1) *Relationship to the Employee Retirement Income Security Act of 1974 and to the Financial Accounting Standards Board.* The Board received a number of comments relative to the relationship between the proposed Standard and the Employee Retirement Income Security Act of 1974 (ERISA). Many of the respondents stated that the proposed Standard contained requirements which are either inconsistent with, more restrictive than, or in conflict with the provisions of ERISA.

The purpose of the Board in promulgating its Standards on pension cost is to establish the criteria for measuring the proper amount of pension cost to be assigned to cost accounting periods for subsequent allocation to negotiated Government contracts. ERISA establishes, among other things, minimum funding Standards for pension plans and provisions affecting deductibility of pension cost for tax purposes. Although there is some commonality between the funding provisions of ERISA and the Standard being promulgated today, ERISA does not provide for the measurement of pension costs for assignment among cost accounting periods or for the subsequent allocation of such costs to contracts.

Notwithstanding the differences in objectives between the proposed Standard and ERISA, the Board believes that compliance with the provisions of the Standard being promulgated today will not violate any provision of ERISA. The Internal Revenue Service confirmed the Board's view on this matter.

One commentator expressed concern over the issuance of a Cost Accounting Standard at this time in view of the active involvement by the Financial Accounting Standards Board in refining the accounting and reporting for both pension plans and employer pension costs. The Board is aware that the FASB may issue a Standard which could be different from the Standard being promulgated today. The Board maintains constant liaison with the FASB with regard to the two Boards' respective responsibilities for developing Standards. It also maintains liaison with the legislative and regulatory bodies responsible for developing and administering ERISA. The Board will review whatever pronouncements these bodies may issue and will consider whether revisions to this Standard are appropriate.

(2) *Definitions.* The Board has received a number of comments relative to the definitions used in the proposed Standard. Some commentators were concerned that the Board is develop-

ing still another glossary of actuarial terms. One of the problems in the field of pension accounting has been the words used to express concepts use. Different meanings have been ascribed to the same terms; different terms have been used to describe the same circumstances; and some terms have inferred meanings which have not been present and have not been intended. Thus, the Board's objective in developing the definitions in this Standard is to help provide a clear understanding of the concepts used therein.

With regard to the specific definitions used in the proposed Standard, the most common problem related to the term "segment." Some commentators construed the term to mean any group of employees performing work for the Government. The definition used in the proposed Standard is the same as that set forth in 4 CFR Part 400. As defined, a segment is an organizational unit which reports directly to a home office of that organization. The designation of organizational units as segments is the responsibility of the contractor; the proposed Standard does not change such designations.

(3) *Assignment of Actuarial Gains and Losses to Cost Accounting Periods.* Section 413.50(a)(2) of the proposed Standard required that for contractors using an immediate-gain actuarial cost method, actuarial gains and losses shall be amortized over a 15-year period. Several commentators stated that immediate recognition of actuarial gains and losses should be required when there are "abnormal forfeitures" (i.e., exceptionally large termination gains). Some commentators expressed a desire for a 10-15-year amortization period; some desired a 10-20-year period; others merely wanted sufficient flexibility to permit them to use whatever amorization period they deem appropriate.

The 15-year amortization period is the same as that set forth in the minimum funding provisions of ERISA. It is also consistent with Opinion No. 8 of the Accounting Principles Board (APB-8) covering the accounting for the cost of pension plans. The Board believes that the amortization period set forth in ERISA is a reasonable basis for adjusting past pension cost accruals without creating significant distortions to current year's accruals. The Board is opposed to the use of various amoritization periods because it would be contrary to the Board's objective of attaining greater consistency and uniformity in the measurement of pension cost and the assignment of such costs to cost accounting periods.

The Board believes also that there is no valid basis for immediate recognition of gains or losses simply because they are exceptionally large. Recognizing gains and losses in the current year generally is not appropriate because the gains or losses are often an adjustment of costs of a number of years. In this regard, the Board notes that APB-8 states also that gains and losses should be recognized immediately only if they arise from a single occurrence not directly related to the operation of the pension plan such as the closing of a plant. The Standard is consistent with this concept. Accordingly the 15-year amortization period has been retained in the Standard being promulgated today.

(4) *Annual calculation of actuarial gains and losses.* A number of commentators objected to the requirement in § 413.40(a) of the proposed Standard that actuarial gains and losses be developed annually. They pointed out that this provision, in effect, requires an annual actuarial valuation. They stated that such a requirement may impose a burden on small contractors, is contrary to ERISA which requires a valuation no less frequently than once every three years, and will result in increased administrative costs.

The Board's primary reason for requiring annual calculations of actuarial gains and losses is to assure that the proper cost is assigned to each cost accounting period. Postponing such calculations may well obscure large fluctuations in pension costs which should be recognized on a timely basis. Because many contracts begin and end within a two or three-year period, such postponements can result in incorrect costs being allocated to these contracts. The Board notes that the overwhelming majority of contractors perform annual actuarial valuations.

In addition, it should be noted that annual actuarial valuations need not be made for all pension plans. Section 412.40(a)(2) of 4 CFR Part 412 provides that for defined-contribution pension plans, the pension cost for a cost accounting period is the net contribution required to be paid for that period. Similarly, § 412.50(a) of 4 CFR Part 412 provides that multiemployer plans, certain insured plans, and certain plans applicable to colleges and universities shall be considered to be defined-contribution pension plans. Accordingly, the requirement to develop actuarial gains and losses annually is not applicable to these plans.

With regard to small contractors, the Board notes that it has not received a single comment from a small contractor stating that the requirement for an annual actuarial valuation for certain pension plans will result in a financial hardship to the contractor. Every comment it has received on this point has come from a major contractor. As for increased actuarial fees, the Board was informed by several actuaries that the difference between the cost of three annual valuations and the cost of a single, three-year valuation is relatively small.

In view of these considerations, the Board has retained the requirement for annual development of actuarial gains and losses.

(5) *Valuation of pension fund assets.* A substantial number of commentators objected to the provision of § 413.50(b)(2) of the proposed Standard which required that the value of pension fund assets be within 80 to 120 percent of the market value of such assets. Some commentators stated that such an approach could have a significant impact on pension cost in a year in which there is a large market fluctuation. Many of these seemed particularly concerned that a substantial drop in the market value of fund assets would cause an increase in pension costs. Other commentators stated that such a requirement is inconsistent with the fundamental requirement of the proposed Standard which stated that the method in use should minimize the effect of short-term market fluctuations. Some suggested various modifications to the proposed Standard to minimize the possible impact of this provision. For example, it was suggested that the average market value of the fund on several dates be used to determine whether an adjustment is required, or that no adjustment should be required unless the value of the fund is outside of the corridor for a period of several years. Some commentators were of the opinion that the corridor approach was reasonable and should be used except in cases where certain asset valuation methods are used; the most common method cited was the 5-year moving average. Several commentators noted that ERISA requires that, for minimum funding purposes, assets shall be valued on a basis which gives consideration to fair market values. They suggested that this provision obviates a need for a corridor.

The Board notes that there is no opposition to the concept that the actuarial value of pension fund assets should take into account the market value of such assets. It recognizes that there are numerous asset valuation methods which take into account market value in varying degrees. In order to achieve an acceptable relationship between the actuarial value of pension fund assets and their market values, the Board could have restricted the use of any of these market valuation methods. In the absence of such restrictions, however, the Board believes some limits must be provided to assure that the actuarial value of fund assets on a given date gives adequate recognition to their market value. The Board reiterates its often stated concept that assignment of costs to the proper period is of paramount importance in determining contract costs. Total reliance on valuation methods which fail to produce actuarial values within the specified corridor is not acceptable for contract costing purposes. For the same reasons, the Board does not accept the suggested modifications to the use of a single asset valuation date because these modifications could defeat the objective of assuring that the value of the fund bears an appropriate relationship to current market values.

The Board notes that the requirement to adjust pension fund assets to within a certain range of market value is not a new concept with this Standard. The Armed Services Procurement Regulations (ASPR) has for many years required that appreciation in equity securities be recognized to the extent that 80 percent of their market value exceeds their adjusted book value. The requirement for upward adjustments of pension fund assets in the Standard being promulgated today is thus similar to the existing ASPR provision. No known problems with this provision for upward adjustments have come to the attention of the Board. Early research in connection with the pension cost Standards did, however, indicate widespread dissatisfaction with the existing ASPR provisions because they did not permit adjustment of pension fund assets below cost. The Standard being promulgated today will correct this apparent inequity.

The Board notes also that many of the commentators apparently did not realize that the adjustment to pension fund assets required pursuant to § 413.50(b) would result in an actuarial gain or loss subject to the 15-year amortization period specified in § 413.50 (a)(2). It should be recognized that the 15-year amortization period minimizes the effect of short-term market fluctuations in two ways. First, the cost impact of the actuarial gain or loss for any year is spread over 15 years. Secondly, in computing a single year's pension cost, there could be adjustments resulting from market fluctuations in as many as 15 prior years. If, as can be expected, some of these adjustments will be increases to the year's pension costs while others will be decreases, the effect of market fluctuations on a year's pension cost will be further minimized. Accordingly, § 413.50(b)(2), in conjunction with § 413.50(a)(2), is considered to assure adequate recognition of the market value of pension fund assets while at the same time assuring that the effect of short-term market fluctuations is minimized.

In summary, the Board continues of the view that wide latitude should be provided for selecting an asset valuation method, but that such latitude should be coupled with the requirement that the assets valued under the method selected fall within a range of the market value of such assets. The requirement that assets be valued at least at 80 percent of market value is consistent with the present provision of ASPR. The requirement that assets be valued at no more than 120 percent of market value is a needed and equitable change to the ASPR concept. These requirements are not expected to result in severe pension cost fluctuations which concerned some of the commentators. Under the circumstances the Board has not adopted those recommendations aimed at deleting or revising the requirement that pension fund assets be valued within 80 to 120 percent of market value.

(6) *Valuation of bonds in a pension fund.* Several commentators expressed their disagreement with the provision of § 413.60(b) of the proposed Standard which required that, in establishing the corridor, market values must be used for all assets, including bonds. They stated that the use of amortized amounts will, over time, produce values less susceptible to short/term market fluctuations than will be produced by the use of market values. They noted also that, for minimum funding purposes, ERISA permits bonds to be valued at cost less amortization. The Board's research shows that assets of a pension fund are acquired for investment purposes and may be liquidated whenever pension fund managers believe that the proceeds therefrom can generate more income elsewhere. The Board's research shows also that the frequent turnover of pension fund assets is the rule rather than the exception. Therefore, the Board continues of the view, that in establishing the corridor, all assets should be valued on the basis of market and no change has been made to § 413.60(b) to provide otherwise. However, the Standard permits a contractor to use amortized values for bonds as a part of the asset valuation method.

(7) *Allocation of pension cost to segments of an organization.* Section 413.40(c) of the proposed Standard provided that pension costs for a segment may always be developed by separate computation. It further provided

that composite pension costs for two or more segments may be computed and allocated by means of an allocation base "unless distortions are created." Section 433.50(c)(2) provided that "unless an equitable allocation of pension costs to segments can be made by means of an allocation base." Separate pension costs for the segment shall be calculated under certain specified conditions.

Some commentators were opposed to a requirement to calculate separate pension costs for a segment under any conditions. Others thought that the proposed Standard was unclear as to when separate segment pension cost calculations were required. A number of commentators concluded that separate calculations would have to be made in any event in order to prove that the use of an allocation base is acceptable. A number of these stated that such separate calculations would be costly.

Normally, pension costs are "central payments or accruals" as that term is used in 4 CFR Part 403. Therefore, where pension costs can be computed for an individual segment, 4 CFR Part 403 would ordinarily require that the amount so computed be the amount allocated to such segment. The calculation of individual segment costs is, in effect, a direct allocation which is not only consistent with CAS 403 but is also consistent with the Board's cost allocation concepts as set forth in the Board's Restatement of Objections, Policies and Concepts (May 1977). Under the circumstances, the Board does not agree with those commentators who are of the view that computation of separate segments pension costs should never be required. Nevertheless, the Board recognizes that the calculation of separate segments pension costs cannot be made without some additional cost and effort. Consistent with its long-standing concepts on materiality, the Board believes that the calculation of separate segment pension cost should be mandatory only when such separate calculations produce materially different results than would result from the use of an allocation base. Therefore the Board sought to provide, in the proposed Standard, criteria to determine when separate calculations would be required.

It is evident that many reviewers of the proposed Standard were uncertain as to when separate segment pension cost calculations would required and when an allocation base could be used. Accordingly, § 413.40(c) has been revised to clearly state that a separate calculation of pension cost for a segment is required only when the conditions set forth in § 413.50(c) (2) and (3) are present. Appropriate changes have also been made in these paragraphs.

The Board recognizes whether separate segment pension cost calculations are required depends in the final analysis on what is considered to be "material" for the purposes of § 413.50(c) (2) and (3). The proposed Standard provided that separate segment costs are to be computed for a segment which had "significant" termination gains; "significantly" different than average benefits, eligibility criteria, or age distribution; or "significantly" different actuarial assumptions.

The concern of many commentators that they would have to make separate segment pension cost calculations in order to prove that the use of a base is acceptable apparently stemmed in part from uncertainty as to what was meant by "significant." The Board is one record as stating that Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of costs. The Board has previously published in its Statement of Operating Policies, Procedures and Objectives certain criteria to be considered in determining whether a transaction or a decision about an accounting practice is material. Such criteria have also been proposed for inclusion in the Board's regulations. It is intended that these criteria be considered in determining whether separate segment pension cost calculations are required.

To clarify that the Board's existing materiality criteria apply in this instance, § 413.50(c) (2) and (3) in the Standard being promulgated today use the words "material" or "materially" in lieu of the words "significant" or "significantly" contained in the proposed Standard. More importantly, a statement has been added to

§ 413.50(c)(2) to state that separate pension cost calculations are required when the listed conditions are present only if "such conditions materially affect the amount of pension costs allocated to the segment." The Board believes that, in most cases, it will be obvious to the contracting parties whether the presence of one or more of these conditions for a segment will materially affect the pension cost for that segment. In cases where the impact is not obviously known, the Board contemplates that the contracting parties will rely on summary estimates as a basis for determining whether separate calculations are required. The Board believes that over time, the need for such summary estimates will diminish. The Board emphasizes that separate calculations are not routinely required, even though no two segments are likely to be identical with respect to the actuarial factors set forth in the Standard. The Board intends that separate segment calculations will be required only in those instances where they would result in a materially different pension cost allocation to a segment.

Several commentators noted that there are pension plans covering several segments that are almost completely devoted to performing work for the Government. Others noted that they had segments which perform a relatively negligible amount of Government work. In either case, according to these commentators, even significant differences in pension cost factors among segments covered by the plan would not materially affect the amount of pension costs allocated to Government contracts. Accordingly, they recommended that the provisions of the Standard relative to separate computations for a segment not be applicable to such segments.

One of the Board's primary objectives in the Standard being promulgated today is to allocate the proper amount of pension costs to each segment. This objective is appropriate, irrespective of the mix of Government and commercial work of a segment or among all segments covered by a pension plan. Even if several segments are entirely devoted to performing work for the Government, the allocation of pension costs among such segment could materially affect the amount of pension costs that are allocated to particular types of contracts in a cost accounting period. The Board recognizes, however, that if a relatively immaterial amount of a segment's work is performed for the Government, any revised allocation of pension cost for that segment would probably have little or no effect on the costs allocated to Government contracts. In such a case, the Board urges the contracting parties give due consideration to the Board's views on materiality.

(8) *Allocation bases.* The proposed Standard required in § 413.50(c)(1) that contractors who compute a composite pension cost for two or more segments must allocate such costs on a base consisting either of the salary and wages of the participants or the number of participants, except where the contracting parties agree to the use of a different base. A number of commentators stated that in certain cases a better beneficial or causal relationship can be obtained by the use of other than the specified bases. The most commonly listed practice was the use of one base to allocate normal cost and another base to allocate unfunded actuarial liabilities. The Board recognizes that in many cases the use of other bases or a combination of bases would provide an equitable means for allocating pension costs to segments. The Board believes that it should not preclude the use of any appropriate base. Therefore, § 413.50(c)(1) of the Standard being promulgated today has been revised to provide that the base to be used for allocating composite pension costs shall be representative of the factors on which the pension benefits are based.

The Board still believes, however, that under certain circumstances, a specific base provides the best means for allocating pension cost. Accordingly, § 413.50(c)(1) still requires the use of salaries and wages as an allocation base where costs are calculated as a percentage of salaries and wages, and the use of a base consisting of the number of employees where costs are calculated as an amount per employee.

(9) *Allocation of pension fund assets to segments.* When pension cost must

be separately calculated for a segment, it will generally be necessary to allocate pension fund assets to such segments. Section 413.50(c)(5)(iii) of the proposed Standard provided that if contractors used different actuarial cost methods in prior years, the allocation of assets must be based on actuarial liabilities developed under the Accrued Benefit actuarial cost method. Several commentators noted that this provision could result in an allocation of assets to segments which is inconsistent with the bases used to accumulate the assets. The Board agrees with this observation. Accordingly, § 413.50(c)(5) of the Standard being promulgated today provides that the allocation of assets shall be made in a manner consistent with the actuarial cost method or methods used to give rise to such assets. It should be noted. however, that such an allocation is permitted only when contributions, disbursements, income, and expenditures made by, or in behalf, of a segment are not readily determinable.

Several commentators suggested that the Standard should be clarified with regard to whether the value of the assets to be allocated shall be the cost of the assets, the actuarial value of the assets, or the market value of the assets. Accordingly, the Board has provided in § 413.50(c)(5)(ii) of the Standard that the allocation shall be the actuarial value of the assets.

Several other commentators expressed concern that the Standard would require that specific assets be allocated to segments. The Board never intended an allocation of specific assets; rather, it intended that there be an initial allocation of assets for accounting purposes only. All of the assets of a pension fund remain available to provide benefit payments for participants in any segment. To clarify this point, § 413.50(c)(5) of the Standard being promulgated today has been revised to state that there shall be an initial allocation of a share in the undivided pension fund assets.

During the course of the Board's research several contractors and actuaries questioned whether the proposed asset allocation requirements prohibited contractors from establishing a separate fund for a segment. The Board does not intend such a prohibition in the Standard being promulgated today.

(10) *Pension costs of inactive participants.* The proposed Standard provided in § 413.50(c)(7) that inactive pension plan participants shall be considered as constituting a separate segment. This provision was included on the basis of research indicating that the accumulation of pension costs applicable to inactive employees would facilitate the allocation of such costs. However, a large number of commentators objected to this provision, stating that it would be much simpler and less costly to merely assign inactive participants to segments. The Board continues to believe that in certain cases the use of a separate segment to accumulate costs applicable to inactive employees will facilitate cost allocation. It recognizes, however, that in other cases assignment of inactive employees to active segments will ease administrative problems. The Board believes that either technique should result in an equitable allocation of pension cost. Accordingly, the Standard being promulgated today specifically provides in § 413.50(c)(9) for the use of either technique.

Section 413.50(c)(10) of the proposed Standard required that the pension cost calculated for the segment created for inactive participant shall be allocated to the active segments on the basis of the pension cost calculated for those segments. Several commentators pointed out that such a basis may be inappropriate in some cases. The Board concurs and has revised § 413.50(c)(9) of the Standard to permit more flexibility in selecting an allocation base under such circumstances.

(11) *Other cost allocation matters.* Several commentators questioned whether contractors must always allocate assets, and continue developing fund data for a segment simply for the purpose of amortizing an identified one-time actuarial gain or loss attributable to a segment. If an equitable allocation of pension cost can be achieved without allocating assets, it is not necessary to do so. For example, in the case of a one-time termination gain or loss, a contractor could isolate

this gain or loss from the other composite actuarial gains or losses and separately credit or charge the former gain or loss over the next fifteen years to the segment from which it arose. The contractor could then continue using the composite cost allocation method (except for such separate adjustment) so long as there is no further unusual experience for that segment. The Board has amended the illustration in § 413.60(c)(1) of the Standard to embody this concept.

Section 413.50(c)(1) of the proposed Standard contained a requirement that costs shall be calculated on a segment basis under circumstances where (1) a pension plan for a segment was, or becomes, merged with that of another segment, and (2) the ratio of assets to actuarial liabilities for each of the merged plans are significantly different from one another after applying the benefits in effect after the merger. In illustrating this point in § 413.36(c)(3), it was indicated that this provision is applicable to mergers which occurred prior to the effective date of the Standard. Several commentators expressed concern over the provision, stating that retroactivity was inequitable. They stated that it would be difficult and expensive to analyze prior years' pension cost, especially in cases where the mergers arose many years ago. The Board believes that these comments have merit. Accordingly, the Standard being promulgated today specifically provides in § 413.50(c)(4) that a requirement for separate segment pension cost calculations for mergers shall have prospective impact only and that pension costs need not be adjusted for prior years. Section 413.60(c)(5) has also been revised.

One commentator noted that its segments performing Government work had different pension cost factors than did the other segments of the company. However, the commentator noted that these factors were homogeneous for the segments performing Government work. The commentator asked whether the Standard requires a separate cost calculation for each segment under such circumstances. The contractor can make a composite calculation for the Government segments and allocate the cost to these segments by means of an allocation base. The contractor can, of course, do this for the other segments. To highlight this point the Board has added an illustration in § 413.60(c)(4) of the Standard.

Two commentators asked whether a difference between the amount of pension cost required to be funded under ERISA, and the sum of the pension costs developed for all segments could be allocated to the various segments. The board recognizes that it is theoretically possible for the sum of all pension costs calculated for segments of an organization to be materially less than the minimum amount required to be funded pursuant to ERISA. However, such a difference may not be assigned to the period for which funding is required. The Board has previously emphasized that the amount of pension cost assignable to a cost accounting period is not necessarily the same as the amount funded for that period. If the amount required to be funded exceeds the amount calculated, the excess amount funded is subject to the provisions of 4 CFR Part 412 (§ 412.50(c)(1)) which states that "Amounts funded in excess of the pension cost computed for a cost accounting period pursuant to the provisions of this Standard shall be applied to pension costs of future cost accounting periods."

(12) *Closing of a segment.* The proposed Standard contained a requirement in § 413.50(c)(13) that when a segment is closed and a significant number of employees are terminated, the contractor shall calculate a gain or loss from the plan applicable to that segment, irrespective of whether the pension plan is terminated. A number of commentators expressed their concern over this provision. Some questioned whether the "net gain or loss" was an actuarial gain or loss and, if so, how it related to other sections of the Standard. Other commentators presumed that this section dealt with the termination of a plan; they stated that, in such an event, the provisions of ERISA and regulations of the Pension Benefit Guarantee Corporation would prevail. They suggested that this section of the Standard be made

applicable only to pension plans that are being continued.

As a general rule, the Standard being promulgated today is based on the concept that material actuarial gains and losses applicable to a segment will be taken into account in future cost accounting periods in determining the costs for the segment. However, a problem arises in cases where a segment is closed. Because there are no future periods in which to adjust previously-determined pension costs applicable to that segment, a means must be developed to provide a basis for adjusting such costs. This adjustment is not an actuarial gain or loss as defined in the Standard. To clarify its intent, the Board has revised § 413.50(c)(12) of the Standard and the related illustration in § 413.60(c)(8). The Standard now states that when a segment is closed, the contractor shall determine the difference between the actuarial liability for the segment and the market value of the assets allocated to the segment.

The Board recognizes that, in some cases, the closing of a segment could be associated with a termination of a plan. Several commentators noted that, in such a case, the actuarial liability for that segment could be greatly influenced by regulations developed pursuant to the provisions of ERISA. The Standard specifically permits the effect of such regulations to be considered in determining the actuarial liability for the segment.

It should be noted that the provisions of this section are appropriate whenever a segment performing a material amount of Government business is closed, irrespective of whether the closing is caused by the completion of a contract or an organizational change, or whether the closing results in a complete or partial termination of the plan. The board emphasizes that the purpose of this provision is to serve as a basis for recognizing and adjusting pension costs previously allocated to the segment being terminated. Such a requirement is independent of whether employees are terminated from the plan.

(13) *Application to defined-contribution and certain other plans.* A number of commentators questioned whether the provisions of the proposed Standard are applicable to defined-contribution and multiemployer pension plans. The Board notes that Standard 412 specifically provides that, for a defined contribution pension plan, the pension cost for a cost accounting period is the net contribution required to be made for that period. Standard 412 provides also that a multiemployer pension plan established pursuant to the terms of a collective bargaining agreement shall be considered to be a defined-contribution pension plan for purposes of this Standard. Thus, the only provisions of this Standard that are applicable to these plans are those dealing with the allocation of costs to segments.

Specific questions were raised with regard to the applicability of the asset valuation requirements to insured plans. Section 413.50(b)(4) of the proposed Standard provided that the asset valuation requirements therein are not applicable to insured plans whose funds are commingled with those of the insurance company. Several commentators stated that this provision was unclear; they questioned whether group deposit administration annuity contracts, immediate participation guarantee contracts, or separate accounts deposit administration contracts are subject to the asset valuation provisions of the Standard. The Board intends that such contracts be subject to these provisions of the Standard. However, the asset valuation provisions do not apply to contracts under which insurance companies guarantee a rate of return. The Board believes that, in such circumstances, the recognition of unrealized appreciation or depreciation on pension fund assets does not alter the basic contractual agreement entered into between the plan sponsor and the insurance company. Section 413.50(b)(4) of the Standard has been revised to clarify this point.

(14) *Costs and benefits.* The anticipated benefits of this Standard are increased consistency and uniformity in measuring actuarial gains and losses and assigning them to cost accounting periods, and better allocation of pension costs to segments of an organization. The Board believes that such im-

proved measurements and allocations will result in more equitable allocation of pension costs to cost objectives, including Government contracts. By providing criteria for controversial aspects of pension cost accounting, the Standard is also expected to reduce disagreements among contracting parties.

In its research leading to the development of this Standard, the Board noted a number of disagreements between contracting parties relating to the disposition of termination gains attributable to segments performing Government contracts. The Board believes that the Standard will diminish, if not eliminate, such disagreements.

On May 19, 1977, the Comptroller General of the United States issued a report to the Congress entitled "Contractor Pension Plan Costs: More Control Could Save the Department of Defense Millions." The General Accounting Office selected, at random, nine Department of Defense prime contractors and examined the pension costs of these contractors. The report states that a substantial amount of questionable pension plan costs were, or may be, charged to Government contracts. The report attributes much of the questionable pension costs to the inequitable allocation of pension plan costs between Government and commercial business. The report states that the Standard being promulgated today deals with, and should correct, many of the problems cited. The following are examples of these problems and the provision of the Standard which deals with them.

(a) A contractor, which calculates pension cost by segment, does not equitably allocate assets to these segments each year; the amounts allocated do not recognize net annual capital contributions by the segments nor the segments shares in the capital growth of pension fund investments. Section 413.50(c) (5), (6) and (7) deals with this subject.

(b) The pension fund of a contractor which acquired a commercial subsidiary is in a surplus position. As a result, pension contributions are not being made for either the Government segments or the commercial subsidiary. Because the surplus was accumulated mainly through Government reimbursements that exceeded the amounts required, the Government's proportional share of the surplus has been diluted by the annual pension plan costs of the commercial subsidiary. Section 413.50(c)(3) deals with this subject.

(c) One contractor used corporate-wide assumptions to calculate pension cost. However, the Government-oriented segments had much higher employee termination rates than did the other segments. The cost to the Government would have been much less if separate pension cost calculations were made for the Government-oriented segments, using the appropriate termination assumptions. Section 413.50(c)(2) deals with this subject.

The Board recognizes that the implementation of this Standard may result in some increased administrative costs by defense contractors. The Board's research shows that any incremental administrative costs incurred will be predominantly related to increased actuarial fees. After discussing with actuaries the nature and scope of increased actuarial work required, the Board is confident that the increased administrative costs required to implement the proposed Standard are relatively small and do not approach the benefits that will be achieved by the proposed Standard.

As required by 719(g) of the Defense Production Act of 1950, as amended, the Board has evaluated the potential inflationary effect of this Standard. The Standard may cause a shift of pension costs from earlier periods to later periods or vice versa. It may also cause a shift of pension costs among various portions of a contractor's business. In the long run, however, total pension costs will not increase or decrease as a result of this Standard. As already noted, increased administrative costs attributable to the Standard are expected to be minimal. Accordingly, the Board concludes that this Standard will have no inflationary effect.

(15) *Effective date.* At the time of promulgation of each previous Standard, the Board followed the policy of reserving the effective date of the Standard, pending the expiration of 60 calendar days of continuous session of the Congress following the date on which the Standard was transmitted. Section 413.80 of the Standard being promulgated today specifies the effective date. The date is included at this time to afford contractors and con-

tracting agencies the earliest possible notification so that they can begin to make implementation plans. In the event any subsequent event makes it necessary to rescind or amend that date, such action will be taken by appropriate notice in the FEDERAL REGISTER.

PART 414—COST ACCOUNTING STANDARD—COST OF MONEY AS AN ELEMENT OF THE COST OF FACILITIES CAPITAL

Sec.
414.10 General applicability.
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414.30 Definitions.
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414.80 Effective date.

APPENDIX A—INSTRUCTIONS FOR FORM CASB-CMF

APPENDIX B—EXAMPLE—ABC CORPORATION

PREAMBLE A

AUTHORITY: Sec. 719 of the Defense Production Act of 1950, as amended, Pub. L. 91-379, 50 U.S.C. App. 2168.

SOURCE: 41 FR 22244, June 2, 1976, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble is intended to explain the regulations in nontechnical language.

§ 414.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (4 CFR 331.30).

§ 414.20 Purpose.

The purpose of this Cost Accounting Standard is to establish criteria for the measurement and allocation of the cost of capital committed to facilities as an element of contract cost. Consistent application of these criteria will improve cost measurement by providing for allocation of cost of contractor investment in facilities capital to negotiated contracts.

§ 414.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Business Unit.* Any segment of an organization, or an entire business organization which is not divided into segments.

(2) *Cost of Capital Committed to Facilities.* An imputed cost determined by applying a cost of money rate to facilities capital.

(3) *Facilities Capital.* The net book value of tangible capital assets and of those intangible capital assets that are subject to amortization.

(4) *Intangible Capital Asset.* An asset that has no physical substance, has more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the benefits it yields.

(5) *Tangible Capital Asset.* An asset that has physical substance, more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the services it yields.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 414.40 Fundamental requirement.

(a) A contractor's facilities capital shall be measured and allocated in accordance with the criteria set forth in this Standard. The allocated amount shall be used as a base to which a cost of money rate is applied.

(b) The cost of money rate shall be based on interest rates determined by the Secretary of the Treasury, pursuant to Pub. L. 92-41 (85 Stat. 97).

(c) The cost of capital committed to facilities shall be separately computed for each of contract using facilities capital cost of money factors computed for each cost accounting period.

§ 414.50 Techniques for application.

(a) The investment base used in computing the cost of money for facilities capital shall be computed from accounting data used for contract cost purposes. The form and instructions stipulated in this Standard shall be used to make the computation.

(b) The cost of money rate for any cost accounting period shall be the arithmetic mean of the interest rates specified by the Secretary of the Treasury pursuant to Pub. L. 92-41 (85 Stat 97). Where the cost of money must be determined on a prospective basis the cost of money rate shall be based on the most recent available rate published by the Secretary of the Treasury.

(c) (1) A facilities capital cost of money factor shall be determined for each indirect cost pool to which a significant amount of facilities capital has been allocated and which is used to allocate indirect costs to final cost objectives.

(2) The facilities capital cost of money factor for an indirect cost pool shall be determined in accordance with Form CASB-CMF, and its instructions which are set forth in Appendix A. One form will serve for all the indirect cost pools of a business unit.

(3) For each CAS-covered contract, the applicable cost of capital committed to facilities for a given cost accounting period is the sum of the products obtained by multiplying the amount of allocation base units (such as direct labor hours, or dollars of total cost input) identified with the contract for the cost accounting period by the facilities capital cost of money factor for the corresponding indirect cost pool. In the case of process cost accounting systems the contracting parties may agree to substitute an appropriate statistical measure for the allocation base units identified with the contract.

§ 414.60 Illustrations.

The use of Form CASB-CMF and other computations anticipated for this Cost Accounting Standard are illustrated in Appendix B.

§ 414.70 Exemptions.

(a) This Standard shall not apply to any prime contract or subcontract providing that (1) the date of award of such contract, or (2) if the contractor has submitted cost or pricing data, the date of final agreement on price as shown on the contractor's signed certificate of current cost or pricing data, precedes the effective date of this Standard.

(b) This Standard shall not apply where compensation for the use of tangible capital assets is based on use rates or allowances such as provided by the provisions of Federal Management Circular 73-8 (Cost Principles for Educational Institutions), Federal Management Circular 74-4 (Principles for Determining Costs Applicable to Grants and Contracts with State and Local Governments), § 15.402-1(a) of the Armed Services Procurement Regulation, or other appropriate Federal procurement regulations.

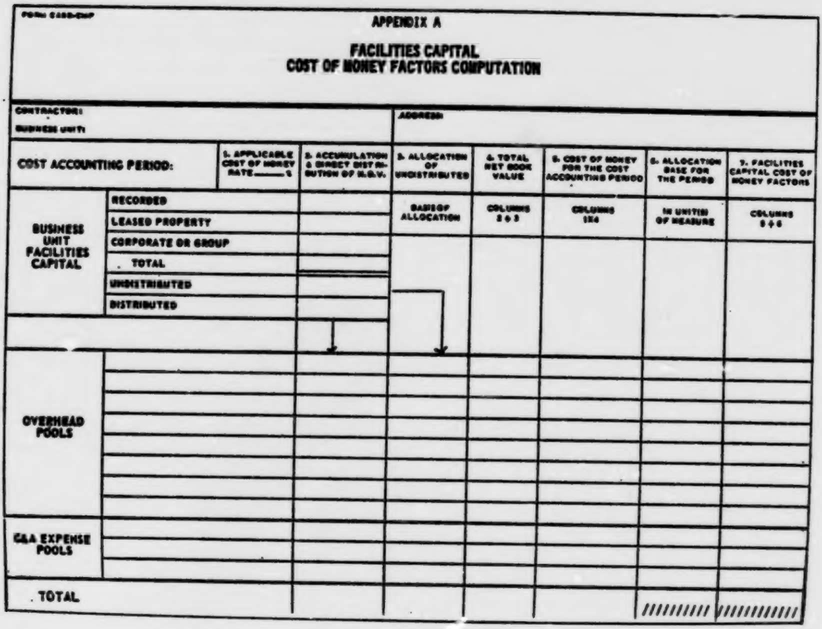
§ 414.80 Effective date.

The effective date of this Cost Accounting Standard is October 1, 1976.

[41 FR 22244, June 2, 1976, as amended at 41 FR 37091, Sept. 2, 1976]

PREAMBLE: Preamble A of the Supplement to Part 401 of this chapter explains how effective dates are determined.

APPENDIX A—INSTRUCTIONS FOR FORM CASB-CMF



FORM CASB-CMF

APPENDIX A

FACILITIES CAPITAL
COST OF MONEY FACTORS COMPUTATION

CONTRACTOR:
BUSINESS UNIT:
ADDRESS:

COST ACCOUNTING PERIOD:	1. APPLICABLE COST OF MONEY RATE ____%	2. ACCUMULATION & DIRECT DISTRIBUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
BUSINESS UNIT FACILITIES CAPITAL	RECORDED		BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1X4	IN UNIT(S) OF MEASURE	COLUMNS 5 ÷ 6
	LEASED PROPERTY						
	CORPORATE OR GROUP						
	TOTAL						
	UNDISTRIBUTED						
	DISTRIBUTED						
OVERHEAD POOLS							
G&A EXPENSE POOLS							
TOTAL						//////////	//////////

Purpose

The purpose of this form is to (a) accumulate total facilities capital net book values allocated to each business unit for the contractor cost accounting period and (b) convert those values to facilities capital cost of money factors applicable to each overhead or G&A expense allocation base employed within a business unit.

Basis

All data pertain to the cost accounting period for which the contractor prepares overhead and G&A expense allocations. The cost of money computations should be compatible with those allocation procedures. More specifically, facilities capital values used should be the same values that are used to generate depreciation or amortization that is allowed for Federal Government contract costing purposes; land which is integral to the regular operation of the business unit shall be included.

Applicable Cost of Money Rate (Col. 1)

Enter here the rate as computed in accordance with § 414.50(b).

Accumulation and Direct Distribution of Net Book Value (Col. 2)

Recorded, Leased Property, Corporate. The net book value of facilities capital items in this column shall represent the average balances outstanding during the cost accounting period. This applies both to items that are subject to periodic depreciation or amortization and also to such items as land that are not subject to periodic write-offs. Unless there is a major fluctuation, it will be adequate to ascertain the net book of these assets at the beginning and end of each cost accounting period, and to compute an average of those two sets of figures. "Recorded" facilities are the facilities capital items owned by the contractor, carried on the books of the business unit and used in its regular business activity. "Leased property" is the capitalized value of leases for which constructive costs of ownership are allowed in lieu of rental costs under Government procurement regulations. Corporate or group facilities are the business unit's allocable share of corporate-owned and leased facilities. The net book value of items of facilities capital which are held or controlled by the home office shall be allocated to the business unit on a basis consistent with the home office expense allocation.

Distributed and Undistributed. All facilities capital items that are identified in the contractor's records as solely applicable to an organizational unit corresponding to a specific overhead, G&A or other indirect cost pool which is used to allocate indirect costs to final cost objectives, are listed against the applicable pools and are classified as "distributed." "Undistributed" is the remainder of the business unit's facilities capital. The sum of "distributed" and "undistributed" must also correspond to the amount shown on the "total" line.

Allocation of Distributed. List in the narrative column all the overhead and G expense pools to which "distributed" facilities capital items have been allocated. Enter the corresponding amounts in (Col. 2). The sum of all the amounts shown against specific overhead and G&A expense pools must correspond to the amount shown in the "distributed" line.

Allocation of Undistributed (Col. 3)

Business unit "undistributed" facilities are allocated to overhead and the G&A expense pools on any reasonable basis that approximates the actual absorption of depreciation or amortization of such facilities. For instance, the basis of allocation of undistributed assets in each business unit between, e.g., engineering overhead pool and the manufacturing overhead pool, should be related to the manner in which the expenses generated by these assets are allocated between the two overhead pools. Detailed analysis of this allocation is not required where essentially the same results can be obtained by other means. Where the cost accounting system for purposes of Government contract costing uses more than one "charging rate" for allocating indirect costs accumulated in a single cost pool, one representative base may be substituted for the multiplicity of bases used in the allocation process. The net book value of service center facilities capital items appropriately allocated should be included in this column. The sum of the entries in Column 3 is equal to the entry in the undistributed line, Column 2.

A supporting work sheet of this allocation should be prepared if there is more than one service center or other similar "intermediate" cost objective involved in the reallocation process.

Alternative Allocation Process—As an alternative to the above allocation process all the undistributed assets for one or more service centers or similar intermediate cost objectives may be allocated to the G&A expense pool. Consequently, the cost of money for these undistributed assets will be distributed to the final cost objectives on the same basis that is used to allocate G&A expense. This procedure may be adopted for any cost accounting period only when the contracting parties agree (a) that the depreciation or amortization generated by these undistributed assets is immaterial or (b) that the results of this alternative procedure are not likely to differ materially from those which would be obtained under the "regular" allocation process described previously.

Total Net Book Value (Col. 4)

The sum of Columns 2 and 3. The total of this column should agree with the business unit's total shown in Column 2.

Cost of Money for the Cost Accounting Period (Col. 5)

Multiply the amounts in Column 4 by the percentage rate in Column 1.

Allocation Base for the Period (Col. 6)

Show here the total units of measure used to allocate overhead and G&A expense pools (e.g., direct labor dollars, machine hours, total cost input, etc.). Include service centers that make charges to final cost objectives. Each base unit-of-measure must be compatible with the bases used for applying overhead in the Federal Government contract cost computation.

The total base unit of measure used for allocation in this column refers to all work done in an organizational unit associated with the indirect cost pool and not to Government work alone.

Facilities Capital Cost of Money Factors (Col. 7)

The quotients of cost of money for the cost accounting period (Col. 5) separtately divided by the corresponding overhead or G&A expense allocation bases (Col. 6). Carry each computation to five decimal places. This factor represents the cost of money applicable to facilities capital allocated to each unit of measure of the overhead or G&A expense allocation base.

APPENDIX B—EXAMPLE—ABC CORPORATION

ABC Corporation has a home office that controls three operating divisions (Business Units A, B & C). The home office includes an administrative computer center whose costs are allocated separately to the business units. The separate allocation conforms to the requirements specified in the Cost Accounting Standard No. 403. Tables I through VI deal with home office expense allocations to business units.

The A Division is a business unit as defined by the CASB, and it uses one engineering and one manufacturing overhead pool to accumulate costs for charging overhead to final cost objectives. In addition the indirect cost allocation process also uses two "service centers" with their own indirect cost pools: occupancy and technical computer center.

The costs accumulated in the occupancy pool are allocated among manufacturing overhead, engineering overhead, and the technical computer center on the basis of floor space occupied. The costs accumulated in the technical computer center cost pool are allocated to users on the basis of a CPU hourly rate. Some of these allocations are made to engineering or manufacturing overhead while others are allocated direct to final cost objectives.

At the business unit level, all the indirect expense incurred is regarded either as an engineering or manufacturing expense. Thus the sole item that enters into the business unit G&A expense pool is the allocation received by the A Division from the home office.

Operating results for the A Division are given in Table VII. Facilities capital items for the division are given in Table IX.

The example is based on a single set of illustrative contract cost data given in Table VIII. Since two methods, the "regular" and the "alternative" method, are potentially available for computing cost of money on facilities capital items two sets of different results can be considered.

In addition, total cost input is used in the example as the allocation base for the G&A expense. Two variations of this example have been prepared to illustrate the impact of excluding or including cost of money from total cost input. Variation I, summarized in Table XIII, excludes cost of money from the cost input allocation base. Variation II, summarized in Tables XVII and XVIII, includes cost of money in the cost input allocation base.

Throughout the example, where appropriate, cross references have been made to the text of the relevant parts of the Standard.

VARIATION I—TOTAL COST INPUT ALLOCATION BASE EXCLUDES COST OF MONEY—TABLE I—*Net book value of home office facilities capital*

	Dec. 31, 1974	Dec. 31, 1975
Administrative computer center facilities capital	$550,000	$450,000
Other home office facilities capital	420,000	380,000
Total	970,000	830,000

The assets in the above table generate allowable depreciation or amortization, as explained in Instructions for Form CASB-CMF (Basis). Thus they should be included in the asset base for cost of money computation.

TABLE II—*Home office facilities capital annual average balances*

Administrative computer center facilities capital	$500,000
Other home office facilities capital	400,000
Total	900,000

The above averages are based on data in Table I computed in accordance with the criteria in Instructions for Form CASB-CMF (Recorded, Leased Property, Corporate).

$970,000+$830,000=$1,800,000÷2=$900,000

TABLE III—*Home office depreciation and amortization for 1975*

Administrative computer center facilities capital	$100,000
Other home office facilities capital	40,000
Total	140,000

TABLE IV—*Allocation of ABC home office expenses to divisions (business units)*

	Total expense	Allocation to business units		
		A	B	C
Administrative computer center	$1,800,000	$900,000	$900,000	
Other home office	4,800,000	2,400,000	1,200,000	$1,200,000
Total	6,600,000	3,300,000	2,100,000	1,200,000

The above allocation is carried out in accordance with 4 CFR Part 403. The expense allocated to individual business units above includes depreciation and amortization as reflected in Table V

TABLE V—*Depreciation and amortization component of ABC home office expense*

	Total depreciation and amortization expense	Allocation to business units		
		A	B	C
Administrative computer center	$100,000	$50,000	$50,000	
Other home office	40,000	20,000	10,000	$10,000
Total	140,000	70,000	60,000	10,000

TABLE VI—*Allocation of home office facilities capital to business units*

(a) Depreciation and amortization allocation in Table V converted to percentages

	Total depreciation and amortization expense (in percent)	Allocation to business units (in percent)		
		A	B	C
Administrative computer center	100	50	50	
Other home office	100	50	25	25

(b) Application of percentages in (a) to average net book values in Table II, in accordance with criteria in Instructions for Form CASB-CMF (Recorded, Leased Property, Corporate).

	Total net book value	Allocation to business units		
		A	B	C
Administrative computer center facilities capital	$500,000	$250,000	$250,000	
Other home office facilities capital	400,000	200,000	100,000	$100,000
Total	900,000	450,000	350,000	100,000

TABLE VII—*"A" division 1975 operating results*

	Total cost input and G. & A.	Fixed price CAS-covered contracts	Cost reimbursement, CAS-covered contracts	Commercial and other work
Direct material:				
Purchased parts	$2,000,000	$100,000	$100,000	$1,800,000
Subcontract items	21,530,000	11,750,000	7,205,000	2,575,000
Total	23,530,000	11,850,000	7,305,000	4,375,000
Direct labor and overhead:				
Engineering labor	2,000,000	1,500,000	500,000	
Engineering overhead (80 pct of direct engineering labor)	1,600,000	1,200,000	400,000	
Manufacturing labor	3,000,000	1,200,000	200,000	1,600,000
Manufacturing overhead (200 pct of direct management labor)	6,000,000	2,400,000	400,000	3,200,000
Other direct charges:				
Technical computer center direct charge—2,280 h at $250/h	570,000	200,000	370,000	
Total cost input (excluding cost of money)	36,700,000	18,350,000	9,175,000	9,175,000
G. & A. (8.99 pct of cost input)	3,300,000	1,650,000	825,000	825,000
Total	40,000,000	20,000,000	10,000,000	10,000,000

TABLE VIII—*Cost data for the contract*

Purchased parts	$85,000
Subcontract items	990,000
Technical computer time 280 h at $250/h	70,000
Engineering labor	330,000
Engineering overhead at 80 pct	264,000
Manufacturing labor	1,210,000
Manufacturing overhead at 200 pct	2,420,000
Total cost input (excluding cost of money)	5,369,000
G. & A. at 8.99 pct	483,000
Total cost input and G. & A. (excluding cost of money)	5,852,000

TABLE IX—*Division A facilities capital*

Average net book values are computed in accordance with Instructions to Form CASB-CMF. Average figures only are given, the underlying beginning and ending balances for 1975 have not been reproduced.

Name of indirect cost pool the asset is associated with	Average net book value	Annual depreciation
Engineering overhead	$320,000	$40,000
Manufacturing overhead	4,500,000	900,000
Technical computer center	450,000	90,000
Occupancy	3,000,000	200,000
Facilities capital recorded by division A (see form CASB-CMF instructions for description of recorded)	8,270,000	1,230,000
Allocated from home office, table VI	450,000	
Total division A	8,720,000	

TABLE X—*Allocation of undistributed facilities capital*

(a) *Occupancy Pool Assets.* Total occupancy pool expenses are assumed tc be $1,000,000 of which $200,000 is depreciation per Table IX. Allocation of the $3,000,000 net book value of assets per Table IX is performed on the basis of floor space utilization.

Indirect cost pool	Occupancy expense and depreciation allocation	Percent of total floor space utilized	Asset allocation
Engineering	$200,000	20	$600,000
Manufacturing	750,000	75	2,250,000
Technical computer	50,000	5	150,000
Total	1,000,000	100	3,000,000

(b) *Technical Computer Center Assets.* Total technical computer center expenses for the year are assumed to be $770,000 including $90,000 depreciation per Table IX and $50,000 charge from the occupancy pool per paragraph (a) of this table. A charging rate of $250 per hour is computed assuming a total of 3,080 chargeable CPU hours per annum. The net book value of assets amounting to $600,000 [$450,000 per Table IX plus the $150,000 allocated per (a) above] is allocated on the basis of CPU hours utilized.

Overhead pool or cost objective	Hours charged	Amount charged	Percent	Asset allocation
Fixed price contracts, table VII	800	$200,000	26	$156,000
Cost reimbursement contracts, table VII	1,480	370,000	48	288,000
Engineering overhead pool	800	200,000	26	156,000
Total	3,080	770,000	100	600,000

(c) *Summary of Undistributed Facilities Capital Allocation.* Undistributed (per Table IX).

Technical computer center	$450,000
Occupancy	3,000,000
Total	3,450,000

Distribution per paragraph (a) or (b) of this table of balances to overhead pools that result in charges direct to final cost objectives.

Overhead pool	(a)	(b)	Total
Engineering	$600,000	$156,000	$756,000
Manufacturing	2,250,000		2,250,000
Technical computer center (direct charge to contracts)		444,000	444,000
Total	2,850,000	600,000	3,450,000

FORM CASB-CMF

TABLE XI

FACILITIES CAPITAL
COST OF MONEY FACTORS COMPUTATION
("Regular" Method - Cost of Money · Excluded from Total Cost Input)

CONTRACTOR: ABC Corp.
BUSINESS UNIT: A Division
ADDRESS:

	COST ACCOUNTING PERIOD: Y.E. 12/31/75	1. APPLICABLE COST OF MONEY RATE 8 %	2. ACCUMULATION & DIRECT DISTRIBUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
BUSINESS UNIT FACILITIES CAPITAL	RECORDED	Table IX	8,270,000	BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1 x 4	IN UNIT(S) OF MEASURE	COLUMNS 5 ÷ 6
	LEASED PROPERTY							
	CORPORATE OR GROUP	Table VI	450,000	Worksheet Table X			Table VII	
	TOTAL		8,720,000					
	UNDISTRIBUTED		3,450,000					
	DISTRIBUTED		5,270,000					
OVERHEAD POOLS	Engineering	Table IX	320,000	756,000	1,076,000	86,080	$2,000,000	.04304
	Manufacturing	Table IX	4,500,000	2,250,000	6,750,000	540,000	$3,000,000	.18
	Technical Computer			444,000	444,000	35,520	2,280 hr	15.57895
G&A EXPENSE POOLS	G&A Expense	Table VI	450,000		450,000	36,000	$36,700,000	.00098
TOTAL			5,270,000	3,450,000	8,720,000	697,600	//////////	////////////

FORM CASB-CMF

TABLE XII

FACILITIES CAPITAL
COST OF MONEY FACTORS COMPUTATION
("Alternative" Method - Cost of Money Excluded from Total Cost Input)

CONTRACTOR: ABC Corp.
BUSINESS UNIT: A Division
ADDRESS:

	COST ACCOUNTING PERIOD: Y.E. 12/31/75	1. APPLICABLE COST OF MONEY RATE 8 %	2. ACCUMULATION & DIRECT DISTRIBUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
BUSINESS UNIT FACILITIES CAPITAL	RECORDED	Table IX	8,270,000	BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1 x 4	IN UNIT(S) OF MEASURE	COLUMNS 5 ÷ 6
	LEASED PROPERTY							
	CORPORATE OR GROUP	Table VI	450,000	All to G&A Expense Pool	-		Table VII	
	TOTAL		8,720,000					
	UNDISTRIBUTED		3,450,000					
	DISTRIBUTED		5,270,000					
OVERHEAD POOLS	Engineering	Table IX	320,000		320,000	25,600	$2,000,000	.0128
	Manufacturing	Table IX	4,500,000		4,500,000	360,000	$3,000,000	.12
G&A EXPENSE POOLS	G&A Expense	Table VI	450,000	3,450,000	3,900,000	312,000	$36,700,000	.00850
TOTAL			5,270,000	3,450,000	8,720,000	697,600	//////////	////////////

TABLE XIII—*Summary of cost of money computation on facilities capital (cost of money excluded from total cost input)*

Allocation base	Allocated to contract table VIII	Computation using regular facilities, capital cost of money factor, table XI	Amount	Computation using alternative facilities capital, cost of money factor, table XII	Amount
Engineering labor	$330,000	0.04304	$14,203	0.0128	$4,224
Manufacturing labor	$1,210,000	.18	217,800	.12	145,200
Technical computer time	[1] 280	15.57895	4,362		
Cost input	$5,369,000	.00098	5,261	.00850	45,636
Total cost of money on facilities capital			241,626		195,060

[1] Hours.

VARIATION II—TOTAL COST INPUT ALLOCATION BASE INCLUDES COST OF MONEY

TABLE XIV—*Recomputation of "A" division total cost input to reflect inclusion of cost of money*

(a) Regular method:	
Total cost input per table VII	$36,700,000
Cost of money applicable to facilities capital identified with overhead pools per subtotal in column 5, table XV	661,600
Total cost input including cost of money	37,361,600
(b) Alternative method:	
Total cost input per table VII	36,700,000
Cost of money applicable to facilities capital identified with overhead pools per subtotal in column 5, table XVI	385,600
Total cost input including cost of money	37,085,900

FORM CASB-CMF

TABLE XV

FACILITIES CAPITAL COST OF MONEY FACTORS COMPUTATION

("Regular" Method - Cost of Money Included in Total Cost Input)

CONTRACTOR: ABC Corp.
BUSINESS UNIT: A Division
ADDRESS:

COST ACCOUNTING PERIOD: Y.E. 12/31/75		1. APPLICABLE COST OF MONEY RATE 8 %	2. ACCUMULATION & DIRECT DISTRIBUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
BUSINESS UNIT FACILITIES CAPITAL	RECORDED	Table IX	8,270,000	BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1X4	IN UNIT(S) OF MEASURE	COLUMNS 5 ÷ 6
	LEASED PROPERTY							
	CORPORATE OR GROUP	Table VI	450,000	Worksheet Table X				
	TOTAL		8,720,000					
	UNDISTRIBUTED		3,450,000				Table VII & Table XIV	
	DISTRIBUTED		5,270,000					
OVERHEAD POOLS	Engineering	Table IX	320,000	756,000	1,076,000	86,080	$2,000,000	.04304
	Manufacturing	Table IX	4,500,000	2,250,000	6,750,000	540,000	$3,000,000	.18
	Technical Computer			444,000	444,000	35,520	2,200 hr	15.57895
	Subtotal: Cost of Money							
	to be included in Total							
	Cost Input					661,600		
G&A EXPENSE POOLS	G&A Expense	Table VI	450,000		450,000	36,000	$37,361,600	.00096
TOTAL			5,270,000	3,450,000	8,720,000	697,600	//////////	//////////

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FORM CASB-CMF

TABLE XVI

FACILITIES CAPITAL COST OF MONEY FACTORS COMPUTATION

("Alternative" Method - Cost of Money Included in Total Cost Input)

CONTRACTOR: ABC Corp.
BUSINESS UNIT: A Division
ADDRESS:

COST ACCOUNTING PERIOD: Y.E. 12/31/75		1. APPLICABLE COST OF MONEY RATE 8 %	2. ACCUMULATION & DIRECT DISTRIBUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
BUSINESS UNIT FACILITIES CAPITAL	RECORDED	Table IX	8,270,000	BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1X4	IN UNIT(S) OF MEASURE	COLUMNS 5 ÷ 6
	LEASED PROPERTY							
	CORPORATE OR GROUP	Table VI	450,000	All to G&A Expense Pool				
	TOTAL		8,720,000				Table VII & Table XIV	
	UNDISTRIBUTED		3,450,000					
	DISTRIBUTED		5,270,000					
OVERHEAD POOLS	Engineering	Table IX	320,000		320,000	25,600	$2,000,000	.0128
	Manufacturing	Table IX	4,500,000		4,500,000	360,000	$3,000,000	.12
	Subtotal: Cost of Money							
	to be included in Total							
	Cost Input					385,600		
G&A EXPENSE POOLS	G&A Expense	Table VI	450,000	3,450,000	3,900,000	312,000	$37,085,600	.00841
TOTAL			5,270,000	3,450,000	8,720,000	697,600	//////////	//////////

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TABLE XVII—*Summary of cost of money computation on facilities capital* (*cost of money included in total cost input—regular method*)

Allocation base	Allocated to contract, table VIII	Computation using regular facilities, capital cost of money factor, table XV	Amount
Engineering labor	$330,000	0.04304	$14,203
Manufacturing labor	$1,210,000	.18	217,800
Technical computer time	[1]280	15.57895	4,362
Cost of money related to overheads			236,365
Cost of money above to be included in cost input	$236,365		
Cost input, table VIII	$5,369,000		
Cost input including cost of money	$5,605,365	.00096	5,381
Total cost of money on facilities capital			241,674

[1] Hours.

TABLE XVIII—*Summary of cost of money computation on facilities capital* (*cost of money included in total cost input—alternative method*)

Allocation base	Allocated to contract, table VIII	Computation using alternative facilities, capital cost of money factor, table XVI	Amount
Engineering labor	$330,000	0.0128	$4,224
Manufacturing labor	1,210,000	.12	145,200
Cost of money related to overheads			149,424
Cost of money above to be included in cost input	$149,424		
Cost input, table VIII	5,369,000		
Cost input including cost of money	$5,518,424	.00841	$46,410
Total cost of money on facilities capital			195,834

PREAMBLE A

Preamble to Original Publication, 6-2-76

The following is the preamble to the original publication of Part 414, 41 FR 22244, June 2, 1976.

The Standard on Cost of Money as an Element of the Cost of Facilities Capital being published today is one of a series being promulgated by the Cost Accounting Standards Board (Board) pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Performance under negotiated contracts usually requires the use of facilities which represent significant contractor investments. Accounting principles applicable to financial reporting do not provide for any explicit recognition of the cost of capital committed to facilities. The Board has long been interested in identifying, as a contract cost, a part of the contractor's total cost of capital. The Board distributed three research papers dealing with the cost of capital in connection with negotiated contracts. These mailings were in June 1974, April 1975, and December 1975. The responses received to all three of those research mailings were useful in the development of the proposal published by the Board on March 5, 1976 (41 FR 9562).

The Board supplemented that March 5 FEDERAL REGISTER request for comments by sending copies of the FEDERAL REGISTER material directly to organizations and individuals who were expected to be interested. The Board has received 82 comments on the March 5 proposal. All of these comments have been carefully considered. The Board appreciates the helpful suggestions and criticisms which have been furnished.

The comments below summarize the major issues discussed by respondents and the significant changes which have been made from the March 5 version of the proposed Standard.

A. GENERAL COMMENTS

(1) *Impact on Contract Prices.* Commentators who represented contractors and the accounting profession tended to favor the proposal, while those who represented some Government agencies were opposed. Government representatives were joined by some other commentators who expressed the belief that the cost of money as an element of the cost of capital committed to facilities should remain, explicit or otherwise, a consideration in determining contract profit compensation, rather than be treated as an element of cost. The Board's early research into the broad question of measurement of the costs related to capital commitment included a number of inquiries about the propriety of a change in the basic concepts of contract cost to include this element.

The cost to be measured, even though imputed, is real and is relevant for contract costing. The Board is persuaded that there has not been adequate agreement on techniques for measuring it. A Cost Accounting Standard is, therefore, appropriate.

Some commentators have expressed concern that contract profit levels may be reduced when this new element of contract cost is recognized, and that there will thus be no real financial benefit from the issuance of the Standard. Such comments are based on a misunderstanding of the Board's mission. The Standard is intended to improve contract cost measurement and understanding by the contracting parties and to provide for greater uniformity by specifying techniques appropriate to types of circumstances actually encountered. Capital asset commitment varies widely among contracts. The Board has developed a technique that takes explicit account of such differences in capital intensity. The procurement agencies are now considering their pricing policies and the Board expects the agencies in doing this to give appropriate recognition to this Standard.

(2) *Exclusion of Working Capital.* As the Board pointed out in its publication on March 5, 1976, its staff has investigated the problems related to measurement of the costs related to investments in operating, or working, capital. Most commentators, while generally favoring the Board's proposal as to the cost of facilities capital, urged that the final promulgation include explicit cost recognition based on the contractor's investment in working capital. The Board is not prepared at this time to make determinations on all the issues related to working capital. The economic impact of contractor investment in facilities is, by itself, important enough to warrant recognition as a contract cost without delay. The Board will seek to resolve the problems related to measurement of the contract cost attributable to the investment in working capital.

(3) *Withdrawal of Proposed CAS No. 413.* A number of commentators expressed regret that the Board had withdrawn its proposed Cost Accounting Standard No. 413 on Adjustment of Historical Depreciation Costs for Inflation, which was published on October 9, 1975. As the Board pointed out in its March 5, 1976 publication, inflation has an impact on interest rates. Research shows that over time there is a strong correlation between interest rates and the rate of change of the price level. The interest rates which were available for measuring the cost of capital would unavoidably include some allowance for inflation. Although a number of respondents denied any overlap, the promulgation of both CAS No. 413 and CAS No. 414 as proposed would have resulted in some duplication of coverage.

The accounting profession continues to consider various approaches to the financial reporting problems related to inflation. The Board will continue to observe the various efforts within the profession, and will consider the usefulness for contract costing purposes of each new statement of generally accepted accounting principles related to inflation.

Should the Board consider it appropriate at some future time to measure the impact of inflation in some other way for contracts, it will, of course, reconsider the rate as well as the method selected for measurement of the cost of money as an element of the cost of facilities capital.

B. CONTENT OF THE STANDARD

(1) *The Renegotiation Board Rate.* The Board's March 5 publication specified the use of the semiannual interest rate established in accordance with Pub. L. 92-41 to serve as a cost of money rate for determining the imputed cost of capital committed to facilities. That law requires that the "rate shall be determined by the Secretary of the Treasury, taking into consideration current private commercial rates of interest for new loans maturing in approximately five years." (section 2, 85 Stat. 97).

Some commentators have pointed out that the interest rate specified under Pub. L. 92-41 was, during 1973-1974, less than the actually experienced rate of general inflation, and thus could not have realistically reflected the rate of inflation. The rate includes provision for the expected impacts of future inflation. In the future as in the past, inflationary expectation may indeed be less than the rate of inflation subsequently experienced; but at times it may also be greater.

Obviously the single interest rate specified under Pub. L. 92-41 and used as a cost of money rate in this Standard will rarely be the precise borrowing rate of any particular contractor.

(2) *Allocation of Facilities.* For contract costing purposes, the cost of capital committed to facilities must be related to contracts. The following three subsections deal with the techniques proposed to establish this relationship.

Simplified Procedure: The Standard being promulgated today is based on allocation to negotiated contracts of an appropriate share of the total cost of money which can be identified with the facilities employees in a business unit. This allocation is made by first identifying the total facilities capital associated with each indirect cost pool. The imputed interest cost is then assigned to contracts on the basis of the same measures used to allocate other costs from those indirect cost pools.

Interested parties almost universally accepted this basic approach. A few have expressed concern, however, that the proposed procedure might entail more effort than would be warranted by the improved precision obtained as compared with a much simpler procedure to approximate the desired allocation.

The March 5 proposal included a provision for a simple allocation technique, based on the established procedure for distribution of G&A expenses. This alternative was to be used "only where the contracting parties agree that the results are not likely to differ materially from those which would be produced under the procedure (otherwise described in the proposed Standard)."

Critics of the proposal suggest that the only way the two parties could agree to use the alternative simple procedure would be to recreate the detail of an allocation using the "regular" method as a comparison. But if the "regular" method must thereby be applied in any case, then there would be no reason to pursue the alternative. The Board has confidence in the reasonableness of the contracting parties in finding ways to achieve the purpose of this Standard. Where the total amount of facilities capital is minor in relation to the estimated incurred cost, for example, the parties could be expected to agree in advance to use the simpler alternative procedure. Similarly, if the contractor has a variety of service centers and other indirect cost pools, which are generally used to serve all productive activities, and which do not individually involve significant facility investments, the alternative procedure could be expected to provide significant administrative convenience, and should probably be used. The situation would be different if a relatively significant portion of the total facilities investment were identified with a service center which is obviously not used with the same intensity for all final cost objectives of the contractor; the imputed cost related to such an investment should be assigned on the basis of the use of the facilities rather than on the basis of some overall allocation procedure.

The instructions in the Standard have been modified slightly to clarify the available flexibility. The Board expects that administrative convenience and the likelihood of significant distortion will be considered in decisions about the use of the simplified alternative procedure permitted.

Basic Allocation Technique. Some commentators criticized the complexity of the regular procedure provided in the March 5 publication. The instructions called for the identification of assets to pools "on any reasonable basis that approximates the actual absorption of depreciation and the related costs of such facilities. The basis of allocation of undistributed assets in each business unit between, for example, the engineering overhead pool and the manufacturing overhead pool, should be related to the manner in which the expenses generated by these assets are absorbed in the two overhead rates. The choice of the basis for allocation is up to the contractor within the limits stated above." Those critics who feel that the instructions require too much detailed analysis in the case of elaborate overhead distribution systems seem not to have understood the intent of the quoted portion. Consolidation and simplification to a limited number of pools and allocation bases is justified in the typical situation where there are many service centers. Minor editorial changes have been made in the instructions, but the Board has not seen the need for any major change in this regard.

Application to Process Cost Systems. The Standard provides a means for allocating the imputed cost to final cost objectives by developing facilities capital cost factors for indirect cost pools. To determine the cost of money applicable to a given final cost objective, these factors must be multiplied by the corresponding allocation base units identified with the final cost objective. A few commentators questioned the technique for applying this procedure for process cost systems.

In a process cost system all the production costs, including overhead costs, are usually accumulated in cost pools associated with "process cost centers" and are then allocated to final cost objectives or products by means of an individual cost center "charging rate." The procedures outlined in this Standard for developing facilities capital cost of money factors for overhead and G&A expense pools are equally applicable to "process cost centers" in case of a process cost system. However, difficulties may arise in computing the appropriate amount of cost of money applicable to each cost objective or product. The difficulties will emerge where the cost records of individual contracts or other final cost objectives do not, as a matter of course, identify any amount of allocation base units related to these final cost objectives in the various "process cost centers." In those circumstances it is anticipated that the contracting parties could agree upon one of several possible acceptable courses of action. Thus it should not be difficult to develop an acceptable allocation basis using statistical methods where appropriate. In addition, the "alternative method," described in instructions to Form CASB-CMF, could be applied in suitable circumstances.

(3) *Inclusion in "Cost Input".* A few commentators questioned whether the imputed cost of capital committed to facilities should be included in the cost input typically to be used as the basis for distribution of G&A expenses under the terms of Cost Accounting Standard No. 410. This element of contract cost is indeed a part of total cost. The term "cost input" is defined as "the cost, except G&A expenses, which for contract costing purposes is allocable to the production of goods and services during a cost accounting period." In principle, the cost of capital committed to facilities, other than those facilities identified with the G&A expense pool, should be included in the total cost input base.

The Board believes that as a practical matter the allocation of the cost of money for the cost accounting period

(See Col. 5 Form CASB-CMF) would not be materially affected by the inclusion or exclusion of cost of money from "cost input." The cost of money for the business unit as a whole would not change. However, to the extent that cost input is used as an allocation base some difference in the allocation to individual contracts can be anticipated. As indicated earlier, however, this difference generally should be immaterial.

In view of the amount of cost accounting data that may be affected by the introduction of cost of money as an element of contract cost and the idiosyncracies of the systems designed to handle that data, the Board believes that administrative expediency should not be ignored. Therefore, at this time it does not prescribe whether this element of cost should be included in or excluded from the cost input allocation base. Although the imputed cost of capital committed to facilities should be included in the total cost input allocation base whenever practicable, exclusion of this element will be acceptable whenever the contractor chooses such exclusion on the basis of reasonable administrative convenience. The illustration in Appendix B is prepared showing the inclusion of this cost and also, as an alternative, showing the exclusion of this element of cost from the measure used as an allocation base for G&A expenses.

C. ADMINISTRATION

(1) *Accounting Records.* The Board's March 5 proposal included the acknowledgement that the imputed cost to be recognized has not been treated under the generally accepted accounting principles applicable to external financial reporting. Even so, several commentators felt the need to point out to the Board that the proposal would involve a cost not currently recognized in published corporate financial reports.

The Board has often emphasized that memorandum records, not necessarily a part of the contractor's formal accounting system, can furnish adequate accounting support for contract purposes, where these purposes differ from those for which the accounting system was developed. The imputed cost to be recognized under this Standard is no exception. The Standard provides the techniques by which this cost will be measured, starting with data already in the accounting records.

(2) *Preparation of Estimates.* The March 5 proposal included the provisions that "where the cost of money must be determined on a prospective basis the cost of money rate shall be based on the most recent available rate published * * *." Some commentators urged that the Standard make more clear the relationship of the published rate to the rate to be used in estimates. Some urged that the published rate be required, and others asked for the publication of official forecasts, which should be used for estimates.

Other commentators pointed out that the determination of the cost of money applicable to a proposed contract requires estimation of a number of asset values and allocation rates. They asked that the Board provide clear instructions as to prospective application.

The Board has never undertaken to advise the contracting parties as to techniques for estimating or for agreeing upon specific amounts of estimated costs. In the case of the imputed cost of capital committed to facilities, as for other elements of cost, the clear determination of the procedure by which "actual" cost will later be measured can eliminate confusion as to the nature of the estimate. The parties may, of course, use any techniques which seem appropriate for agreeing on the numeric values to be included in contract cost estimates.

(3) *Compliance with Standard No. 401.* The Board has earlier promulgated a Standard (4 CFR Part 401) which requires that the practices used in pricing a proposal (estimating) shall be consistent with the cost accounting practices used in accumulating and reporting costs. One of the essential features of that Standard is the requirement that any significant element of cost in the estimate can be compared with the corresponding actual cost. A number of commentators have expressed concern about the applicabil-

ity of that Standard to an imputed cost.

For the purposes of complying with Standard No. 401 the Board believes that any reasonable estimating technique which establishes the cost of money as a separate amount is acceptable. It is not necessary in estimating to follow precisely the procedures, including Form CASB-CMF, incorporated in the Standard.

D. APPLICABILITY

(1) *Use Rates.* Contractors are sometimes compensated for the use of facilities by means of "use rates" authorized under Government procurement policies. These rates may cover various elements of ownership costs, including depreciation. The March 5 publication contained a proposed exemption for situations where such use charges were included in contract costs. A number of commentators criticized that proposed exemption.

The Board does not intend to interfere with the process of establishing "use rates" nor is it prepared to define at this time the factors that should be taken into account when they are formulated. The Board believes that the cost of money is a valid economic cost, and that it is as relevant to a contractor employing a use rate as it is to one using depreciation. Existing schedules of use rates have presumably included appropriate consideration of all elements of the total cost to be considered in developing such rates. The proposed exemption for those covered by use charges is accordingly retained.

(2) *Existing Covered Contracts.* Many commentators urged revision of § 414.70 of the March 5 proposal to delete the exemption of contracts and subcontracts entered into prior to the effective date of the Standard. Such contracts were negotiated under the provisions of Government procurement regulations. In all such regulations, any interest costs incurred by the contractor have been specifically designated as unallowable costs. Furthermore, none of these regulations has recognized any imputed cost of capital committed to facilities. The agreement of the parties, embodied in such prior contracts, has necessarily been reached in light of the cost principles existing at the time the contracts were entered into. The Board therefore concludes that this Standard should not be applied to existing contracts and the Board has consequently retained the exemption in § 414.70.

E. BENEFITS AND COSTS

With respect to Cost Accounting Standards, the Board's primary goal is to issue clearly stated Standards to achieve (1) an increased degree of uniformity in accounting practices among Government contractors and (2) consistency in accounting treatment of costs by individual Government contractors. Increased uniformity and consistency are desirable to the extent that they improve understanding and communication.

Contract costs currently do not include any measurement of the cost of money, which is undeniably a cost related to contract performance. The result is that contract cost measurements have made no distinction between contracts with equal amounts of total incurred cost but with vast differences in amounts of facilities investment.

This Standard need have no impact in the aggregate prices paid by the Government but will reflect specific identifiable cost of money as an element of the cost of facilities capital in individual negotiated contracts. Previously, these costs presumably were reflected in nonidentifiable amounts in the profits or fees included in the total contract prices. By reflecting specific costs of money attributable to contractor investments in facilities, this Standard will provide for greater consistency in negotiating total contract prices. The Board understands that procurement agencies expect to take this Standard into account in their current reconsideration of pricing policies. The Standard also will assist the procurement agencies to discriminate more effectively between contracts in which the cost of money is significant and those in which it is not.

The Nation's mobilization base depends on its facilities. These may be more effectively modernized because of the explicit cost recognition provided by this Standard, which will help to eliminate the existing disincentives which have hampered contractor investments in facilities. Also, to the extent that the Standard results in investment in cost-reducing equipment, the Government will be able to procure goods and services at lower prices.

Some commentators have suggested that the Board's issuance of Cost Accounting Standard No. 409 caused the need for recognition of this element of cost of facilities capital, and that the Standard being promulgated should be judged in that context. The Board does not agree. The Standard on depreciation was justified by the need for improved criteria with respect to depreciation expense identified with contract performance. Some critics of that Standard argued, in effect, that it should not have been promulgated because, even though it would improve depreciation accounting, there were economic costs not yet being recognized, and that improper depreciation could be justified as an acceptable technique for meeting the economic need. The Board was not and is not persuaded by such reasoning.

The Board has considered the administrative costs related to implementation of this Standard. The most significant potential problems mentioned by commentators were related to features of the proposal which have been modified in response to those comments. The Standard as promulgated today is not expected to involve any significant administrative difficulty, either for contractors or for the Government.

In summary, the Board finds that the benefits of this Standard, which are significant, outweigh the costs, including any inflationary impact.

F. MISCELLANEOUS

The Board expects that this Standard will become effective on October 1, 1976.

There is also being published today an amendment to Part 400, *Definitions*, to incorporate in that part terms defined in § 414.30(a) of this Cost Accounting Standard.

PART 415—ACCOUNTING FOR THE COST OF DEFERRED COMPENSATION

Sec.
415.10 General applicability.
415.20 Purpose.
415.30 Definition.
415.40 Fundamental requirement.
415.50 Techniques for application.
415.60 Illustrations.
415.70 Exemption.
415.80 Effective date.
PREAMBLES A—B

AUTHORITY: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

SOURCE: 41 FR 31799, July 30, 1976, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble is intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (41 FR 31799, July 30, 1976) is set forth as Preamble A of the supplement.

For preambles to amendments and revisions which affect only certain sections, see the references following those sections.

§ 415.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards in negotiated defense prime contracts and subcontracts (4 CFR 331.30).

§ 415.20 Purpose.

(a) The purpose of this Standard is to provide criteria for the measurement of the cost of deferred compensation and the assignment of such cost to cost accounting periods. The application of these criteria should increase the probability that the cost of deferred compensation is allocated to cost objectives in a uniform and consistent manner.

(b) This Standard is applicable to the cost of all deferred compensation except for compensated personal absence and pension plan costs which are covered in other Cost Accounting Standards.

§ 415.30 Definition.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section:

(1) *Deferred Compensation.* An award made by an employer to compensate an employee in a future cost accounting period or periods for services rendered in one or more cost accounting periods prior to the date of the receipt of compensation by the employee. This definition shall not include the amount of year end accruals for salaries, wages, or bonuses that are to be paid within a reasonable period of time after the end of a cost accounting period.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 415.40 Fundamental requirement.

(a) The cost of deferred compensation shall be assigned to the cost accounting period in which the contractor incurs an obligation to compensate the employee. In the event no obligation is incurred prior to payment, the cost of deferred compensation shall be the amount paid and shall be assigned to the cost accounting period in which the payment is made.

(b) The measurement of the amount of the cost of deferred compensation shall be the present value of the future benefits to be paid by the contractor.

(c) The cost of each award of deferred compensation shall be considered separately for purposes of measurement and assignment of such costs to cost accounting periods. However, if the cost of deferred compensation for the employees covered by a deferred compensation plan can be measured with reasonable accuracy on a group basis, separate computations for each employee are not required.

§ 415.50 Techniques for application.

(a) The contractor shall be deemed to have incurred an obligation for the cost of deferred compensation when all of the following conditions have been met. However, for awards which require that the employee perform future service in order to receive the benefits, the obligation is deemed to have been incurred as the future service is performed for that part of the award attributable to such future service.

(1) There is a requirement to make the future payment(s) which the contractor cannot unilaterally avoid.

(2) The deferred compensation award is to be satisfied by a future payment of money, other assets, or shares of stock of the contractor.

(3) The amount of the future payment can be measured with reasonable accuracy.

(4) The recipient of the award is known.

(5) If the terms of the award require that certain events must occur before an employee is entitled to receive the benefits, there is a reasonable probability that such events will occur.

(6) For stock options, there must be a reasonable probability that the options ultimately will be exercised.

(b) If any of the conditions in § 415.50(a) is not met, the cost of deferred compensation shall be assignable only to the cost accounting period or periods in which the compensation is paid to the employee.

(c) If the cost of deferred compensation can be estimated with reasonable accuracy on a group basis, including consideration of probable forfeitures, such estimate may be used as the basis for measuring and assigning the present value of future benefits.

(d) The following provisions are applicable for plans that meet the conditions of § 415.50(a) and the compensation is to be paid in money.

(1) If the deferred compensation award provides that the amount to be paid shall include the principal of the award plus interest at a rate fixed at the date of award, such interest shall be included in the computation of the amount of the future benefit. If no interest is included in the award, the

amount of the future benefit is the amount of the award.

(2) If the deferred compensation award provides for payment of principal plus interest at a rate not fixed at the time of award but based on a specified index which is determinable in each applicable cost accounting period, e.g., a published corporate bond rate, such interest shall be included in the computation of the amount of future benefit. The interest rate to be used shall be the rate in effect at the close of the period in which the cost of deferred compensation is assignable. Since that interest rate is likely to vary from the actual rates in future periods, adjustments shall be made in any such future period in which the variation in rates materially affects the cost of deferred compensation.

(3) If the deferred compensation award provides for payment of principal plus interest at a rate not based on a specified index or not determinable in each applicable year:

(i) The cost of deferred compensation for the principal of the award shall be measured by the present value of the future benefits of the principal and shall be assigned to the cost accounting period in which the employer incurs an obligation to compensate the employee and

(ii) The interest on such awards shall be assigned to the cost accounting period(s) in which the payment of the deferred compensation is made.

(4) If the terms of the award require that the employee perform future service in order to receive benefits, the cost of the deferred compensation shall be appropriately assigned to the periods of current and future service based on the facts and circumstances of the award. The cost of deferred compensation for each cost accounting period shall be the present value of the future benefits of the deferred compensation calculated as of the end of each such period to which such cost is assigned.

(5) In computing the present value of the future benefits, the discount rate shall be equal to the interest rate as determined by the Secretary of the Treasury pursuant to Pub. L. 92-41, 85 Stat. 97, at the time the cost is assignable.

(6) If the award is made under a plan which requires irrevocable funding for payment to the employee in a future cost accounting period together with all interest earned thereon, the amount assignable to the period of award shall be the amount irrevocably funded.

(7) In computing the assignable cost for a cost accounting period, any forfeitures which reduce the employer's obligation for payment of deferred compensation shall be a reduction of contract costs in the period in which the forfeiture occurred. The amount of the reduction for a forfeiture shall be the amount of the award that was assigned to a prior period, plus interest compounded annually, using the same Treasury rate that was used as the discount rate at the time the cost was assigned. For irrevocably funded plans, pursuant to § 415.50(d)(6), the amount of the reduction for a forfeiture shall be the amount initially funded plus or minus a pro-rata share of the gains and losses of the fund.

(8) If the cost of deferred compensation for group plans measured in accordance with § 415.50(c) is determined to be greater than the amounts initially assigned because the forfeiture was overestimated, the additional cost shall be assignable to the cost accounting period in which such cost is ascertainable.

(e) The following provisions are applicable for plans that meet the conditions of § 415.50(a) and the compensation is received by the employee in other than money. The measurements set forth herein constitute the present value of future benefits for awards made in other than money and, therefore, shall be deemed to be a reasonable measure of the amount of the future payment.

(1) If the award is made in the stock of the contractor, the cost of deferred compensation for such awards shall be based on the market value of the stock on the measurement date, i.e., the first date the number of shares awarded is known. Market value is the current or prevailing price of the security as indicated by market quotations. If such values are unavailable or not appropri-

ate (thin market, volatile price movements, etc.) an acceptable alternative is the fair value of the stock.

(2) If an award is made in the form of options to employees to purchase stock of the contractor, the cost of deferred compensation of such award shall be the amount by which the market value of the stock exceeds the option price multiplied by the number of shares awarded on the measurement date, i.e., the first date on which both the option price and the number of shares is known. If the option price on the measurement date is equal to or greater than the market value of the stock, no cost shall be deemed to have been incurred for contract costing purposes.

(3) If the terms of an award of stock or stock option require that the employee perform future service in order to receive the stock or to exercise the option, the cost of the deferred compensation shall be appropriately assigned to the periods of current and future service based on the facts and circumstances of the award. The cost to be assigned shall be the value of the stock or stock option at the measurement date as prescribed in § 415.50(e)(1) or (e)(2).

(4) If an award is made in the form of an asset other than cash, the cost of deferred compensation for such award shall be based on the market value of the asset at the time the award is made. If a market value is not available, the fair value of the asset shall be used.

(5) If the terms of an award, made in the form of an asset other than cash, require that the employee perform future service in order to receive the asset, the cost of the deferred compensation shall be appropriately assigned to the periods of current and future service based on the facts and circumstances of the award. The cost to be assigned shall be the value of the asset at the time of award as prescribed in § 415.50(e)(4).

(6) In computing the assignable cost for a cost accounting period, any forfeitures which reduce the employer's obligation for payment of deferred compensation shall be a reduction of contract costs in the period in which the forfeiture occurred. The amount of the reduction shall be equal to the amount of the award that was assigned to a prior period, plus interest compounded annually, using the Treasury rate (see § 415.50(d)(5)) that was in effect at the time the cost was assigned. If the recipient of the award of stock options voluntarily fails to exercise such options, such failure shall not constitute a forfeiture under provisions of this Standard.

(7) Stock option awards or any other form of stock purchase plans containing all of the following characteristics shall be considered noncompensatory and not covered by this Standard:

(i) Substantially all full-time employees meeting limited employment qualifications may participate,

(ii) Stock is offered to eligible employees equally or based on a uniform percentage of salary or wages,

(iii) An option or a purchase right must be exercisable within a reasonable period, and

(iv) The discount from the market price of the stock is no greater than would be reasonable in an offer of stock to stockholders or others.

§ 415.60 Illustrations.

(a) Contractor A has a deferred compensation plan in which all cash awards are increased each year by an interest factor equivalent to the long-term borrowing rate of the contractor prevailing during each such year. The interest factor based on a variable long-term borrowing rate meets the criteria of § 415.50(d)(2). Consequently, the cost of deferred compensation for Contractor A shall be measured by the present value of the future benefits and shall be assigned to the cost accounting period in which the contractor initially incurs an obligation to compensate the employee. If the long-term borrowing rate for Contractor A was nine percent at the close of the period to which the cost of deferred compensation was assignable, then that rate should be used to calculate the future benefit. Any adjustment in the cost of deferred compensation which results from a material change in the nine percent rate in future applicable periods shall be made in each such future period or periods (see § 415.50(d)(2)).

(b) Contractor B made a deferred compensation award of $10,000 to an employee on December 31, 1976, for services performed in 1976 to be paid in equal annual payments of $2,000 starting at December 31, 1981. The terms of the award do not provide for an interest factor to be included in the payment; consequently, according to provisions of § 415.50(d)(1), interest may not be included in the computation of the future benefit. The assignable cost for 1976 is computed as follows, assuming that the interest rate determined by the Secretary of the Treasury (pursuant to Pub. L. 92-41, 85 Stat. 97) at the time of award is eight percent and the conditions set forth in § 415.50(a) are met.

Year	Amount of future payment×Discount rate 8-pct present value factor=Present value
1981	$2,000×0.6805=$1,361
1982	2,000×.6301= 1,260
1983	2,000×.5834= 1,167
1984	2,000×.5402= 1,080
1985	2,000×.5002= 1,000
Assignable cost for 1976	5,868

(c) Contractor C awarded stock options for 1,000 shares of the contractor to key employees on December 31, 1976, under a deferred compensation plan requiring two years of additional service before the awards can be exercised. The facts and circumstances of the awards indicate that the deferred compensation applies only to the periods of future service. The market price of the stock was $26 per share, the option price was $22, and the interest rate established by the Secretary of the Treasury in effect at the time of award was 8 percent.

(1) In accordance with § 415.50(e)(2), the cost of the stock options is the amount by which the current value of the stock exceeds the option price multiplied by the number of shares awarded on the measurement date. Thus, the total cost of the stock options is 1,000 shares multiplied by the difference of the option price and the market price ($26−22) or $4,000.

(2) Under provisions of § 415.50(e)(3), the cost for stock options is assigned to each future cost accounting period in which employee service is required and is computed as follows:

	Assignable Cost[1]
Year of required service:	
1977	$2,000
1978	2,000
Total amount of award	4,000

[1] Note that this illustration assumes that the facts and circumstances of the award indicate that the award relates equally to each period of future service. Thus, the assignable cost was allocated on a pro-rata basis.

(d) (1) Contractor D has a deferred compensation plan that specifies that an employee receiving a cash award must remain with the company for three calendar years after the award in order to qualify and receive the award and the facts and circumstances indicate that the deferred compensation applies only to the periods of future service. In accordance with § 415.50(d)(4), the cost of deferred compensation is assignable to the periods of future service. Thus, the amount of cost of deferred compensation to be assigned by Contractor D for each of the three years shall be the present value of the future benefits of the deferred compensation award calculated as of the end of each such period to which such cost is assigned.

(2) Under this plan, Contractor D made an award to an employee of $3,000 to be paid at the end of the third year. The assignable cost for each of the three years is computed as follows:

Year[1]	Amount of future payment	×	Present value factor[2] using prevailing Treasury rate[3]	=	Assignable cost for each year
1	$1,000	×	0.8573 (8 pct for 2 yr)	=	$857.30
2	1,000	×	0.9302 (7.5 pct for 1 yr)	=	930.20
3	1,000	×	1.000 (8 pct for 0 yr)	=	1,000.00

[1] Note that in accordance with the facts and circumstances of the award no deferred compensation is assignable to the period in which the award is made and that the award relates equally to each period of future service.

[2] Note that since the costs are measured at the end of each year of required service, the present value factors are based on the number of years from the year of assignment to the date of payment.

[3] Note that the prevailing Treasury rate changed from year 1 to year 2.

(e) (1) Contractor E has a deferred compensation plan that specifies that an employee receiving a cash award must remain with the company for two calendar years after the award in order to qualify and receive the award. Contractor E made an award of $6,000 at the end of 1976 to an employee to be paid at the end of 1978. However, the employee voluntarily terminated his employment before the end of 1977. The facts and circumstances of the award indicate that $2,000 of the award represents compensation for services rendered in the period of award (1976). The remaining portion of the award represents compensation for services to be rendered in future periods. The assignable cost for 1976, which was the only period to which costs were assigned before termination, was the present value of $2,000, the amount of the award attributable to the services of that period. Thus, the cost assigned for 1976 was:

Amount of future payment × Discount rate present value factor for 2 yr at 8 pct = Assignable cost

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$2,000 × 0.8573 = $1,714.60

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(2) According to provisions of § 415.50(d)(7), the amount of the forfeiture shall be the amount of the cost that was assigned to a prior period, plus interest compounded annually, from the year the cost was assigned to the year of forfeiture, using the same Treasury rate (see § 415.50(d)(5)) that was used as the discount rate at the time the cost was assigned. The Treasury rate in effect at the date of award was eight percent.

(3) The amount of the forfeiture is computed as follows:

Assignable cost × Discount rate future value factor for 1 yr at 8 pct = Forfeiture

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$1,714.60 × 1.08 = $1,851.77

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§ 415.70 Exemption.

None for this Standard.

§ 415.80 Effective date.

(a) The effective date of this standard is July 10, 1977.

(b) This standard shall be followed by each contractor for awards of deferred compensation made on or after the start of his next cost accounting period beginning after the receipt of a contract to which the cost accounting standard is applicable.

[43 FR 24821, June 8, 1978]

PREAMBLE: For preamble, see preamble B of the supplement to this part.

PREAMBLE A

Preamble to Original Publication, 7-30-76

The following is the preamble to the original publication of Part 415, 41 FR 31797, July 30, 1976.

The Standard on Accounting for the Cost of Deferred Compensation being published today is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. This Standard provides criteria for the measurement of the cost of deferred compensation and the assignment of such cost to cost accounting periods.

Early research included an extensive review of available literature, the Disclosure Statements filed with the Board, and decisions of boards of contract appeals. This information was then supplemented by visits and mail solicitations to contractors in order to elicit more specific data concerning company deferred compensation plans.

In May 1975, a questionnaire/issues paper was sent to a wide mailing list soliciting responses to several basic issues identified in the Board's early research. Seventy responses to the questionnaire/issues paper were received from interested parties, the majority of whom were companies that had deferred compensation plans. Based on the responses received, a preliminary draft Standard was developed in December 1975 and sent to a large cross section of companies, Government agencies, industry and professional associations, and other interested individuals. The Board received 53 responses to the draft Standard.

After several changes were made to the draft Standard, based on consideration of the comments made by respondents, a proposed Standard was published in the FEDERAL REGISTER of April 7, 1976, with an invitation to interested parties to submit written views and comments to the Board.

The Board received 34 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms and others in response to the FEDERAL REGISTER proposal. All of these comments have been carefully considered by the Board. The Board's views on each of the major issues discussed by the commentators are outlined in the following sections, together with explanations of the changes made in the Cost Accounting Standard being promulgated.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions it has received and the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

RELATIONSHIP OF STANDARD TO CURRENT PROCUREMENT REGULATIONS

Under current procurement regulations, deferred compensation is allocable as a cost of Government contracts only to the extent that such costs are deductible for the same fiscal year for Federal income tax purposes. A few commentators expressed concern that the proposed Standard would require the assignment of the cost of deferred compensation to a cost accounting period that would be different than that determined under the Internal Revenue Code for Federal income tax purposes.

Under the Internal Revenue Code, a deduction for tax purposes for the cost of many incentive or bonus type plans is not permitted until the deferred compensation is paid to the recipient. Under the Standard, however, the cost of deferred compensation is assignable as a contract cost in the period the contractor incurs an obligation to pay such cost which, for many deferred compensation plans, will be the period in which the award is made. (See § 415.40(a).)

The Board has recognized that contract costing often deals with the same expenditures as are of interest in income tax accounting. Except for differences in tax rates, shifts of income or expense from one year to another generally do not have a significant effect on total tax paid over a period of time. Similar shifts of cost, however, from one year to another could have a decided impact on the costs chargeable to Government contracts. This impact occurs because the mix of Government and commercial contracts often changes significantly from period to period. Therefore, the Board believes that application of the criteria provided in the Standard to assign the cost of deferred compensation on an accrual basis of accounting is needed to better assure that such cost of deferred compensation will be assigned to appropriate cost accounting periods.

ALLOCABILITY AND ALLOWABILITY OF CONTRACT COSTS

Several Government agency commentators pointed out that under present procurement regulations deferred compensation is not allowable until the period in which paid. These commentators also noted that the cost of stock options, under present procurement regulations, is unallowable. Although these commentators gener-

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ally recognized that the provisions of the Standard involve allocability, they questioned whether the Standard would encroach on the allowability prerogatives of the procurement agencies.

The Board believes that recognition of the cost accounting concept that all costs incurred in carrying on the activities of an enterprise are allocable to the cost objectives of the enterprise is essential to the maintenance of sound and consistent contract cost accounting. Cost Accounting Standards should result in determination of costs which are allocable to contracts and other cost objectives. The use of Cost Accounting Standards, however, has no direct bearing on allowability determinations.

DEFINITION

A commentator was concerned that the proposed Standard may apply to the cost of some pension plans that are subject to Accounting Principles Board Opinion No. 8, Accounting for the Cost of Pension Plans, and that different measures of cost might result for the same plan from application of the proposed Standard and from application of APB Opinion No. 8. The commentator questioned whether an amount paid to an employee after retirement for a specified period of time, e.g., 10 years, would fall under the definition of deferred compensation as used in this Standard. If a payment for a specified period of time after retirement is, in effect, equivalent to a life income settlement, this payment falls within the definition of a pension plan as provided in Cost Accounting Standard 412, Composition and Measurement of Pension Cost. If the payment is not a life income settlement, it is not a pension plan and the award is covered under the definition of deferred compensation. The Board does not believe that the Standard being promulgated today applies to any pension plan covered under APB Opinion No. 8.

DETERMINATION OF OBLIGATION

One of the criteria contained in the Standard for determining whether a contractor has incurred an obligation for the cost of deferred compensation is whether or not there is reasonable probability that certain required conditions precedent will occur before an employee is entitled to receive the benefits (see § 415.50(a)(5)). The proposed Standard stated that, in determining whether certain events are likely to occur, one of the factors to be considered was the reasonableness of the time interval between the award and the expected occurrence of the event. A few commentators suggested that the proposed Standard specify the length of time that would be reasonable. The Board does not believe that a particular time period can be specified to cover all circumstances. Each category of award must be analyzed on a case-by-case basis because there are several factors involved in determining whether employees should be entitled to receive the benefits of an award. Among the factors that should be considered, in addition to the time interval, are the employer's experience with similar awards and other restrictive terms which may be involved in the terms of the award.

Since there are numerous factors to be considered, the Board has deleted from § 415.50(a)(5) of the Standard mention of two specific factors in order not to give undue weight to these factors. In addition, the Board has added § 415.50(a)(6) to make clear with respect to stock options, that an obligation is deemed to have been incurred only if there is a reasonable probability that the option ultimately will be exercised.

FUTURE SERVICE REQUIREMENTS

Section 415.50(a)(3) provides, as a condition for the assignment of deferred compensation, that the amount of future payment be capable of being measured with reasonable accuracy. In this connection, several commentators suggested that this provision should override the provision for prorating the cost if future service is required. The commentators stated that the service to be rendered after the period of award does not influence the basis for the award. These commentators believe that if there is a strong likelihood that the recipients of the awards would remain with the company for the periods of future service then the costs should be charged in the year of award.

The Board does not agree that the reasonable accuracy of measuring the cost should override the appropriate assignment of the cost to the periods of current and future service based on the facts and circumstances of the award. The Board believes that, where future service is required, such compensation related to the service rendered in those future periods and therefore the related cost should be assigned to those periods. In this regard, the Board believes that the concepts embodied in Accounting Principles Board Opinion No. 12 Omnibus Opinion, are appropriate for contract costing. This Opinion states that "If elements of both current and future service are present [for deferred compensation awards], only the portion applicable to the current service should be accrued." To make certain that this concept is clearly understood to be incorporated in the Standard being promulgated, a provision has been added to § 415.50(a).

VARIABLE INTEREST RATE

Several commentators expressed concern over a provision in the proposed Standard which stated that if the interest rate included in the award is not fixed at the date of award, the interest was to be assignable only to the periods in which the interest was paid. A few of these commentators stated that generally accepted accounting principles require that the estimated amount to be paid should be assigned in a systematic and rational manner. The commentators stated that, if the amount of interest is known in each period, it should be assigned in each such period.

The Board agrees that the variable interests amounts should be assigned to periods in a systematic and rational manner provided that the terms of the plan specify the basis under which variable interest amounts will be derived and the interest applied in each period is determinable at that time. Consequently, the Standard being promulgated today has been revised to provide in § 415.50(d)(2), that variable interest included in awards shall be assigned in the same period as the principal of the award, provided that the rate is based on a specified index and is determinable in each applicable period. The Standard also provides that since the interest rate used at the time of the award is likely to vary from the actual rates in future periods, adjustments shall be made in any future period in which the variation in rates materially affects the cost of deferred compensation.

Section 415.50(d)(3) was added to the Standard to provide for those situations in which the interest rate was not based on a specified index or not determinable in each applicable year. In these situations, the present value of the principal amount of the award is assignable in the year of award and the interest cost is assignable to the period or periods in which the payments are made.

FORFEITURES

Two commentators stated that the forfeiture provision should be expanded to recognize that losses on the initial payment for irrevocably funded plans, as well as earnings, may occur within the framework of such a plan. The Board had intended that both gains and losses be recognized and has changed the provision to clarify this point (see § 415.50 (d)(7)).

Another commentator stated that the forfeiture provision should not include interest to the date of the forfeiture. The commentator stated that it seems inequitable to require that the value of the forfeiture be determined at a level which was not fully allowable as a cost during the accounting periods affected. The Board does not share the view that including interest in the credit for forfeitures is inequitable. The interest factor represents the time cost of money which the contractor should pay to the Government for having been provided with funds. The forfeiture is calculated to be the present value of the future benefit at the time of forfeiture and thus is equivalent in present value terms to the amount of deferred compensation that was originally assigned. However, as stated in the Standard, the failure of the recipient to volun-

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tarily exercise a stock option is not considered a forfeiture.

The Standard has been amended to provide that if a recipient of an award of stock options voluntarily fails to exercise such options, such failure does not constitute a forfeiture. (See § 415.50(e) (6).)

STOCK AND STOCK OPTIONS

A few commentators cited the requirement of § 415.50(a)(3) of the proposed Standard which provides that the amount of the future payment must be capable of reasonable estimation, and expressed their opinion that the value of award of contractor stock that is to be distributed in a future period or periods should not be assigned to any period prior to payment because the amount of payment to the employee cannot be reasonably estimated before that time.

The Board believes that the compensation cost of stock or stock option plans should be measured by the quoted market price of the stock at the measurement date less the amount, if any, that the employee is required to pay. Further, the measurement date for both stock awards and stock option plans should be the first date on which are known both the number of shares to be distributed and the option price, if any. These views are embodied in Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, which already must be followed by contractors for financial reporting.

If the market price of the stock on the date of distribution is used, the Government, in effect, would be sharing in financial risk-taking with the contractor. Subsequent fluctuations of the price of the stock should not influence the measurement of the award. However, the Board recognized that the proposed Standard was not consistent with respect to the measurement of the cost of stock and stock option. Consequently, § 415.50(e)(1) has been changed to provide for the measurement of the cost of stock to be at the measurement date rather than the time an obligation was deemed to have been incurred.

In order to further clarify the Board's intent, § 415.50(e) had been revised to provide that the measurement of the award of stock, stock options, or other assets as set forth in the Standard shall be deemed to be a reasonable measure of the amount of the future payment.

Two commentators stated that the cost of stock options should be based on the value of the options on the date they are exercised. Similar to the reasoning expressed above, the Board does not believe that it would be appropriate to base the cost of stock options on the value prevailing at the date of exercise. Stock options which are awarded at a value which equals the market value of the stock would involve no cost under the provisions of the Standard. However, if the award of stock options were based on their value at the date exercised, a cost of the award would have to be recognized by the Government even though the contractor could purchase an appropriate number of shares at the time of the award to defray any cost resulting from future increases in the market value of the stock. The Board believes, therefore, that stock options should be measured at the date on which both the option price and the number of shares are established (see § 415.50(e)(1)).

Several commentators suggested that the requirement for prorating the cost of stock options over the period of future service and taking the present value of the prorated cost should be eliminated because the price of the stock is the present value of the stock price. The Board agrees with these commentators. Consequently, the requirement for discounting the cost of stock options has been eliminated from the Standard.

TRANSITION PROVISION

Several commentators suggested that a transition provision be included in the Standard to amortize costs of deferred compensation accumulated in periods prior to the promulgation of the Standard, but not previously charged to contract costs. Several of these commentators suggested various methods to amortize the recovery of all prior deferred compensation on an accelerated basis. Among the methods suggested was to charge all such prior costs in the period that the Standard became effective or to charge such costs over the remaining work life of the employee or five years, whichever is shorter. However, one commentator recommended that the Board use a suspense account, as used in Cost Accounting Standard 408, Accounting for Cost of Compensated Personal Absence. The use of a suspense account would delay recognition of the cost of deferred compensation awarded before the effective date of the Standard.

The procurement regulations for costs of deferred compensation awarded prior to the effective date of the Standard generally provide that such costs will be allocable in the period in which they are paid to recipients. The Standard being promulgated today would not disturb the contractual provisions applicable to such prior awards. The provisions of this Standard are applicable only to new awards of deferred compensation made on or after the date that the Standard becomes applicable to each contractor. The Board recognizes that there will be a minor budgetary increase required by the Government agencies until the prior deferred compensation awards are paid. However, for the majority of deferred compensation plans, the awards previously made will be paid out over a relatively short period of time, e.g., five years. Consequently, the Board believes that a transition provision is not necessary for the Standard being promulgated today.

OTHER CHANGES

The first illustration (§ 415.60(a)) was changed to reflect the change in the provision regarding interest rates that are not fixed at the date of award. Other changes of a minor nature were made to various sections of the Standard for clarification.

COSTS AND BENEFITS

Section 719(g) of the Defense Production Act of 1950, as amended, provides "In promulgating such standards and major rules and regulations for the implementation of such standards, the Board shall take into account, and shall report to the Congress in the transmittal required by section 719(h)(3) hereof, the probable costs of implementation, including inflationary effects, if any, compared to the probable benefits, including advantages and improvements in the pricing, administration and settlement of contracts."

Comments received in response to the FEDERAL REGISTER publication, as well as information obtained from contractors prior thereto, indicated that there would be minimal administrative costs entailed in complying with the Standard. One Government agency stated that additional administrative burden would be placed on the Government as a result of the conversion from a cash basis to the accrual method of accounting. The Board believes that any such additional administrative costs due to this conversion will be minimal. The Governmental agencies have always had the responsibility for reviewing the reasonableness of deferred compensation plans and evaluating the payments to assure that such payments coincide with the principal and interest provisions of the plan. The Board believes the main additional administrative cost involved is in reviewing the present value calculation and determining if the contractor has incurred a valid obligation at the time the award is made.

Among the benefits which the Board believes will be derived from the use of this Standard is the assignment of the costs of deferred compensation to proper periods. Under the present regulations, the assignment of much of these costs is essentially on a cash basis. As a consequence, deferred compensation costs may have been incurred in much earlier periods than the periods in which they were recognized as incurred costs; in many cases, several years after the service has been rendered by the employee. Giving full consideration to all the relevant factors discussed herein, the Board believes the benefits to be derived from this Standard clearly outweigh any costs of implementation.

As required by section 719(g), the Board has evaluated the potential inflationary effect of this Standard. The Standard requires the use of present value techniques for the assignment of cost and incorporates a forfeiture provision with interest. The use of these

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techniques recognizes the time cost of money. In the long run, the cost to the Government should be essentially the same as that which would be incurred under a cash basis of accounting. For a majority of deferred compensation plans, moreover, the awards previously made will be paid out over a relatively short period of time, e.g., five years. The Board has concluded that there will be only a minor budgetary increase on the Government agencies until the prior deferred compensation awards are paid. Overall, however, any inflationary effect of this Standard will be minimal.

The Board expects that this Standard will become effective January 1, 1977.

There is also being published today an Amendment to Part 400, Definitions, to incorporate in that part terms defined in § 415.30 of this Cost Accounting Standard.

PREAMBLE B

Preamble to Revision of Section, 7-30-76 and 1-8-78

The following is the preamble to the revision of § 415.80, published at 42 FR 18857, Apr. 11, 1977 and correctly reprinted at 43 FR 24821, June 8, 1978.

On July 30, 1976, a Cost Accounting Standard entitled Accounting for the Cost of Deferred Compensation was published in the FEDERAL REGISTER (41 FR 31797 et seq.). The effective date of the Standard was reserved in the July 30 publication. This final rule establishes the effective date.

PART 416—ACCOUNTING FOR INSURANCE COSTS

Sec.

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PREAMBLE A

AUTHORITY: 84 Stat. 796, Sec. 103, 50 U.S.C. App. 2168.

SOURCE: 43 FR 42239, Sept. 20, 1978, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble, is intended to explain the regulations in nontechnical language.

The preamble to the originial publication of thir part (43 FR 42239, Sept. 20, 1978) is set forth in preamble A of the supplement.

§ 416.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (4 CFR 331.30).

§ 416.20 Purpose.

The purpose of this standard is to provide criteria for the measurement of insurance costs, the assignment of such costs to cost accounting periods, and their allocation to cost objectives. The application of these criteria should increase the probability that insurance costs are allocated to cost objectives in a uniform and consistent manner.

§ 416.30 Definitions.

(a) The following definitions of terms which are prominent in this standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

Actual cash value. The cost of replacing damaged property with other property of like kind and quality in the physical condition of the property immediately prior to the damage.

Insurance administration expenses. The contractor's costs of administering an insurance program, e.g., the costs of operating an insurance or risk-management department, processing claims, actuarial fees, and service fees paid to insurance companies, trustees, or technical consultants.

Projected average loss. The estimated long-term average loss per period for periods of comparable exposure to risk of loss.

Self-insurance. The assumption or retention of the risk of loss by the contractor, whether voluntarily or involuntarily. Self-insurance includes the deductible portion of purchased insurance.

Self-insurance charge. A cost which represents the projected average loss under a self-insurance plan.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this standard: None.

§ 416.40 Fundamental requirement.

(a) The amount of insurance cost to be assigned to a cost accounting period is the projected average loss for that period plus insurance administration expenses in that period.

(b) The allocation of insurance costs to cost objectives shall be based on the beneficial or causal relationship between the insurance costs and the benefiting or causing cost objectives.

§ 416.50 Techniques for application.

(a) *Measurement of projected average loss.*

(1) For exposure to risk of loss which is covered by the purchase of insurance or by payments to a trusteed fund, the premium or payment, adjusted in accordance with the following criteria, shall represent the projected average loss:

(i) The premium cost applicable to a given policy term shall be assigned pro rata among the cost accounting periods covered by the policy term, except as provided in paragraphs (a)(1)(ii) through (vi) of this section. A refund, dividend or additional assessment shall become an adjustment to the pro rata premium costs for the earliest cost accounting period in which the refund or dividend is actually or constructively received or in which the additional assessment is payable.

(ii) Where insurance is purchased specifically for, and directly allocated to, a single final cost objective, the premium need not be prorated among cost accounting periods.

(iii) Any part of a premium or payment to an insurer or trustee, or any part of a dividend or premium refund retained by an insurer or trustee which would be includable as a deposit in published financial statements prepared in accordance with generally accepted accounting principles shall be accounted for as a deposit for the purpose of determining insurance costs.

(iv) Any part of a premium or payment to an insurer or to a trustee, or any part of a dividend or premium refund retained by an insurer, for inclusion in a reserve or fund established and maintained on behalf of the insured or the policyholder or trustor, shall be accounted for as a deposit unless the following conditions are met:

(A) The objectives of the reserve or fund are clearly stated in writing;

(B) Measurement of the amount required for the reserve or fund is actuarially determined and is consistent with the objectives of the reserve or fund;

(C) Payments and additions to the reserve or fund are made in a systematic and consistent manner; and

(D) If payments to accomplish the stated objectives of the reserve or fund are made from a source other than the reserve or fund, the payments into the reserve or fund are reduced accordingly.

(v) If an objective of an insurance program is to prefund insurance coverage on retired persons, then, in addition to the requirements imposed by paragraph (a)(1)(iv) of this section:

(A) Payments must be made to an insurer or trustee to establish and maintain a fund or reserve for that purpose;

(B) The policyholder or trustor must have no right of recapture of the reserve or fund so long as any active or retired participant in the program remains alive unless the interests of such remaining participants are satisfied through adequate reinsurance or otherwise; and

(C) The amount added to the reserve or fund in any cost accounting period must not be greater than an amount which would be required to apportion the cost of the insurance coverage fairly over the working lives of the

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active employees in the plan. If a contractor establishes a terminal-funded plan for retired persons or converts from a pay-as-you-go plan to a terminal-funded plan, the actuarial present value of benefits applicable to employees already retired shall be amortized over a period of 15 years.

(vi) The contractor may adopt and consistently follow a practice of determining insurance costs based on the estimated premium and assessments net of estimated refunds and dividends. If this practice is adopted, then any difference between an estimated and actual refund, dividend, or assessment shall become an adjustment to the pro rata net premium costs for the earliest cost accounting period in which the refund or dividend is actually or constructively received or in which the additional assessment is payable.

(2) For exposure to risk of loss which is not covered by the purchase of insurance or by payments to a trusteed fund, the contractor shall follow a program of self-insurance accounting according to the following criteria:

(i) Except as provided in paragraph (a)(2) (ii) and (iii) of this section actual losses shall not become a part of insurance costs. Instead, the contractor shall make a self-insurance charge for each period for each type of self-insured risk which shall represent the projected average loss for that period. If insurance could be purchased against the self-insured risk, the cost of such insurance may be used as an estimate of the projected average loss; if this method is used, the self-insurance charge plus insurance administration expenses may be equal to, but shall not exceed, the cost of comparable purchased insurance plus the associated insurance administration expenses. However, the contractor's actual loss experience shall be evaluated regularly, and self-insurance charges for subsequent periods shall reflect such experience in the same manner as would purchased insurance. If insurance could not be purchased against the self-insured risk, the amount of the self-insurance charge for each period shall be based on the contractor's experience, relevant industry experience, and anticipated conditions in accordance with accepted actuarial principles.

(ii) Where it is probable that the actual amount of losses which will occur in a cost accounting period will not differ significantly from the projected average loss for that period, the actual amount of losses in that period may be considered to represent the projected average loss for that period in lieu of a self-insurance charge.

(iii) Under self-insurance programs for retired persons, only actual losses shall be considered to represent the projected average loss unless a reserve or fund is established in accordance with § 416.50(a)(1)(v).

(iv) The self-insurance charge shall be determined in a manner which will give appropriate recognition to any indemnification agreement which exists between the contracting parties.

(3) In measuring actual losses under paragraph (a)(2) of this section:

(i) The amount of a loss shall be measured by (A) The actual cash value of property destroyed; (B) amounts paid or accrued to repair damage; (C) amounts paid or accrued to estates and beneficiaries; and (D) amounts paid or accrued to compensate claimants, including subrogation. Where the amount of a loss which is represented by a liability to a third party is uncertain, the estimate of the loss shall be the amount which would be includable as an accrued liability in financial statements prepared in accordance with generally accepted accounting principles.

(ii) If a loss has been incurred and the amount of the liability to a claimant is fixed or reasonably certain, but actual payment of the liability will not take place for more than 1 year after the loss is incurred, the amount of the loss to be recognized currently shall not exceed the present value of the future payments, determined by using a discount rate equal to that prescribed for settling such claims by the State having jurisdiction over the claim. If no such rate is prescribed by the State, then the rate shall be equal to the interest rate as determined by the Secretary of the Treasury pursuant to Pub. L. 92-41, 85 Stat. 97, in effect at the time the loss is recognized. Alternatively, where settlement will consist of a series of payments over an indefinite time period, as in worker's compensation, the contractor may follow a consistent policy of recognizing only the actual amounts paid in the period of payment.

(4) The contractor may elect to recognize immaterial amounts of self-insured losses or insurance administration expenses as part of other expense categories rather than as "insurance costs."

(b) *Allocation of insurance costs:* (1) Where actual losses are recognized as an estimate of the projected average loss, in accordance with § 416.50(a)(2), or where actual loss experience is determined for the purpose of developing self-insurance charges by segment, a loss which is incurred in a given segment shall be identified with that segment. However, if the contractor's home office is, in effect, a reinsurer of its segments against catastrophic losses, a portion of such catastrophic losses shall be allocated to, or identified with, the home office.

(2) Insurance costs shall be allocated on the basis of the factors used to determine the premium, assessment, refund, dividend, or self-insurance charge, except that insurance costs incurred by a segment or allocated to a segment from a home office may be combined with costs of other indirect cost pools if the resultant allocation to each final cost objective is substantially the same as it would have been if separately allocated under this provision.

(3) Insurance administration expenses which are material in relation to total insurance costs shall be allocated on the same basis as the related premium costs or self-insurance charge.

(c) *Records.* The contractor shall maintain such records as may be necessary to substantiate the amounts of premiums, refunds, dividends, losses, and self-insurance charges, paid or accrued, and the measurement and allocation of insurance costs. Memorandum records may be used to reflect any material differences between insurance costs as determined in accordance with this standard and as includable in financial statements prepared in accordance with generally accepted accounting principles.

§ 416.60 Illustrations.

(a) Contractor A pays a companywide property and casualty insurance premium for the policy term July 1, 1980, to July 1, 1983, and includes the entire amount as cost in its cost accounting period which ended December 31, 1980. This is a violation of § 416.50(a)(1)(i) in that only one-sixth of the policy term fell within the cost accounting period which ended December 31, 1980, and therefore only one-sixth of the premium should have been included in cost in that cost accounting period.

(b) Contractor B has a retrospectively rated worker's compensation insurance program. The policy term corresponds with the contractor's cost accounting period. Premium refunds are normally received and applied in the following cost accounting period. The contractor's practice is to include the entire gross premium in insurance cost in the cost accounting period in which it is paid and to credit the refund against insurance cost in the cost accounting period in which it is received. This practice conforms with § 416.50(a)(1)(i). The contractor could also, under the provisions of § 416.50(a)(1)(vi), have followed a consistent practice of estimating such refunds in advance and including the estimated net premium in insurance cost.

(c) Contractor C establishes a self-insured program of life insurance for active and retired persons. The contractor pays death benefits directly to the beneficiaries of deceased employees and includes such payments in insurance costs at the time of payment. This practice complies with § 416.50(a)(2)(iii) which requires that only the actual losses be recognized unless a trusteed reserve or fund is established in accordance with § 416.50(a)(1)(v).

(d) Instead of paying death benefits directly, contractor D purchases annual group term life insurance on active and retired persons and charges the premiums to insurance costs (with proper recognition for refunds and dividends). Contractor D's retired persons wish to be protected against possible discontinuance of the program. Contractor D, therefore, establishes a trusteed fund. As each employee retires, contractor D deposits in the fund an amount which is equal to the premium on a paid-up policy for that employee, and he advises the trustee that the fund is to be used to continue to pay premiums on retired persons in the event the program is discontinued. The contractor also continues to purchase group term insurance on both active employees and retired persons and charges both the premiums and the deposits to insurance costs. This practice does not comply with § 416.50(a)(1)(iv)(D) which requires that if payments to accomplish the stated objectives of the reserve or funds are made from a source other than the reserve or fund, the payments into the fund shall be reduced accordingly.

NOTE: In this instance the contractor could comply with the standard by paying from the fund that portion of the group term premium which represented the retired persons or by reducing the deposits to the fund by an equivalent amount in accordance with § 416.50(a)(1)(iv)(D). This practice would also comply with the requirement of § 416.50(a)(1)(v)(C) that the amount added to the fund not be greater than an amount which would be required to fairly allocate the cost over the working lives of the active employees in the plan.

(e) Contractor E wishes to provide assurance of his life insurance program continuance to both active and retired employees. He establishes a trusteed fund in accordance with § 416.50(a)(1) (iv) and (v) and thereafter pays into the fund each year for each active employee an actuarially determined amount which will accumulate to the equivalent of the premium on a paid-up life insurance policy at retirement. He charges the annual payments to insurance costs. Benefits are paid directly from the fund (or the fund is used to pay the annual premiums on group term life insurance for all employees). This practice also complies with the requirement of § 416.50(a)(1)(v)(C) that the amount added to the fund not be greater than an amount which would be required to fairly allocate the cost over the working lives of the active employees in the plan.

(f) Contractor F has a fire insurance policy which provides that the first $50,000 of any fire loss will be borne by the contractor. Because the risk of loss is dispersed among many physical units of property and the average potential loss per unit is relatively low, the actual losses in any period may be expected not to differ significantly from the projected average loss. Therefore, the contractor intends to let the actual losses represent the projected average loss for this exposure to risk. Property with an actual cash value of $80,000 is destroyed in a fire. The contractor charges the $50,000 of the loss not covered by the policy to insurance costs for contract costing purposes. The practice complies with the requirement of § 416.50(a)(2). However, had the contractor's plan been to make a self-insurance charge for such losses, then any difference between the self-insurance charge and actual losses in that cost accounting period would not have been allocable as an insurance cost.

(g) Contractor G is preparing to enter into a Government contract to produce explosive devices. The contractor is unable to purchase adequate insurance protection and must act as a self-insurer. There is a significant possibility of a major loss, against which the Government will not undertake to idemnify the contractor. The contractor, therefore, intends to make a self-insurance charge for this exposure to risk. The contractor may, in accordance with § 416.50(a)(2)(i), use data obtained from other contractors or any other reasonable method of estimating the projected average loss in order to determine the self-insurance charge.

(h) Contractor H purchases liability insurance for all of its motor vehicles in a single, company-wide policy which contains a $50,000 deductible provision. However, the company's management policy provides that when a loss is incurred in a segment, only the first $5,000 of the loss will be charged to the segment; the balance of the loss will be absorbed at the home-office level and reallocated among all segments. Because the risk of loss is dispersed among many physical units and the maximum potential loss per occurrence is limited, the actual losses in any cost accounting period may be expected not to differ significantly from the projected average loss. Therefore, the contractor intends to let the actual losses represent the projected average loss for this exposure to risk. An analysis of the loss experience shows that many past losses exceeded $5,000. Contractor H's practice of allocating the loss in excess of $5,000 to the home office is a violation of § 416.50(b)(1)(ii). The limit of $5,000 cannot realistically be considered a measure of a "catastrophic" loss when losses frequently exceed this amount, and the use of a limit this low would obscure segment loss experience.

§ 416.70 Exemptions.

None for this standard.

§ 416.80 Effective date.

(a) The effective date of this standard is July 10, 1979.

(b) This standard shall be followed by each contractor on or after the start of his next cost accounting period beginning after the receipt of a contract to which this cost accounting standard is applicable.

PREAMBLE A

Preamble to Original Publication, 9-20-78

The following is the preamble to the original publication of Part 416, 43 FR 42239, Sept. 20, 1978.

(1) BACKGROUND

Work on a potential standard on accounting for insurance costs was initiated for a number of reasons; these included (1) differences between armed services procurement regulation (ASPR) provisions governing self-insurance and Financial Accounting Standards Board (FASB) statement No. 5, (2) Armed Services Board of Contract Appeals (ASBCA) cases or other disputes related to insurance accounting, and (3) knowledge of unresolved problems obtained by discussions with contractors and audit agencies.

A statement of issues related to accounting for insurance and a preliminary draft standard were developed by the staff and circulated to contractors, agencies, and others. Responses to these staff papers and to the FEDERAL REGISTER publications of October 5, 1977, and May 15, 1978, and information obtained in subsequent meetings with respondents and other interested persons were considered in developing the standard which is being promulgated today. Twenty-nine comments were received in response to the most recent FEDERAL REGISTER publication All comments have been considered by the Board and those addressing areas of significance are discussed below, together with explanations of the changes made in the cost accounting standard being promulgated today from the proposal published in the FEDERAL REGISTER of May 15, 1978.

Ten respondents said that the proposed standard was acceptable as written, or they suggested only minor word changes.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(2) COVERAGE OF STANDARD

One respondent said that the standard should be limited in its application to significant problem areas rather than treating all insurance and insurance-related costs in a general fashion. As stated in the prefatory remarks which accompanied the May 15, 1978, FEDERAL REGISTER publication, in its research, the Board did not find that accounting practices depended upon the type of risk or insurance. Therefore this standard, applicable to the major problems, is also appropriate for all other insurance.

One respondent suggested that the standard deal with the subject of premiums paid to "captive" insurers. The Board reiterates its belief, which it stated in the May 15, 1978, FEDERAL REGISTER publication, that the technique for accounting for premium costs should not be influenced by questions of the reasonableness of the amounts paid. Consequently, no change in this regard has been made in the May 15, 1978, proposal.

(3) SELF-INSURANCE AS A COST

Three respondents suggested that the proposed standard failed to properly distinguish between self-insurance and the absence of insurance. The Board recognizes that there may indeed be differences in the amount of planning involved, but there is no difference in the principle applicable to cost measurement. "Absence of insurance" is in fact one kind of self-insurance. The respondents said that a contractor who does not purchase insurance or set up a funded reserve to cover possible losses does not incur a cost and that, in such situations, actual losses are a part of entrepreneurial risk taking and should come directly from profit. For the reasons set forth below the Board does not agree.

A contractor who acquires assets is exposed to two types of risks—static risks and dynamic risks. Static risks are the risks which are inherent in the ownership of the assets; dynamic risks result from the decision to utilize the assets for the production of specific goods or services. Static risks are the same for all owners of similar assets in similar circumstances; e.g., the risk that property of a given type in a given location will be destroyed or damaged. Consequently, they are normally predictable by mathematical methods and can be insured against. Dynamic risks are a function of managerial judgment, e.g., whether a proposed product can be produced for a profit. Dynamic risks are not normally predictable or insurable; they generate a profit or loss, depending on management's ability to forecast costs and markets; they are the true entrepreneurial risks. Static risks, because they can be measured, predicted, and quantified, are properly subject to treatment as costs rather than as entrepreneurial risks.

From a cost accounting standpoint, the decision to purchase insurance or self-insure is not one of cost versus no-cost. Rather, it is one of certainty versus uncertainty. A contractor who self-insures will be subject to cost variations in any short time period as compared to one who purchases insurance, but in the long run their costs should be substantially the same and their product or service must be priced to cover the same long-term cost.

Whether a contractor should be required to make deposits in a fund to provide for replacement of assets in the event of loss is not a consideration in determining the costs of self-insurance.

(4) ACCOUNTING FOR SELF-INSURANCE

When the business entity purchases insurance coverage from an underwriter, the cost to the business—for the static risk—is the premium. When the business entity does not purchase insurance, the best method of assignment of cost to current activities is a matter of possible disagreement.

A contractor who self-insures can recognize the cost of self-insurance for product pricing purposes in either of two ways:

(1) By recognizing actual losses as they occur and allocating them to the products of some time period, usually the cost accounting period in which the loss occurred; or (2) by estimating the long-term average loss per time period and allocating it to the products of each time period. The second method is conceptually preferable in that it allocates the costs of all losses to the products of all time periods without regard to the particular chance distribution of actual losses among time periods.

The proposals which were published in the October 5, 1977, and May 15, 1978, FEDERAL REGISTER included criteria for selecting between the two approaches to recognizing the cost of self-insurance. A charge which would represent the projected average loss was required except in those situations where the actual losses in a cost accounting period could be expected to serve as a good representative of the long-term average loss for that period. The recognition of actual losses, rather than the use of a predeterminated charge, would be expected where many units are exposed to loss and the maximum loss related to any one unit would be relatively small. Examples are the losses falling within the deductible portion of the automobile collision coverage for a fleet of vehicles, the deductible portions of property and casualty coverage where the size of the deductible is nominal in relation to the total exposure to risk for that coverage, and the worker's compensation claims of a large work force. There would be little point in calculating a special self-insurance charge in such circumstances.

The Board has decided to retain the requirement for the use of a self-insurance charge, as contained in the FEDERAL REGISTER proposal. A reasonable assignment of cost should be made to products of each period in which there is exposure to the risk. The cost of each loss should be allocated to all work accomplished in the facility where it occurred (and successor facilities over the life of the enterprise, not just to the work of the day, month, or year in which the loss happened to occur. This can be accomplished by charging each period with a self-insurance charge which is equal to the projected average loss.

The standard also retains the provision of the FEDERAL REGISTER proposals which permitted the recognition of actual losses in those limited circumstances, as described above, in which the actual losses in any cost accounting period may be expected not to differ significantly from the projected average loss for that period.

Several respondents were concerned as to the possible consequences if a self-insurance charge were to be made, and, subsequently, actual losses differed substantially from the projected average loss. The self-insurance charge is, of necessity, and estimate. If the estimate is made in a reasonable and supportable manner, then the fact that actual losses depart significantly in either direction from the projected average loss is not a basis for adjusting the costs of that cost accounting period. However, the standard provides that contractor's actual loss experience shall be reviewed regularly and that self-insurance charges for subsequent periods shall reflect experience, as would premiums for purchased insurance. Similarly, if the situation were one in which it had been determined that actual losses were to be used because they were not expected to differ significantly from the projected average loss, and actual losses did, in fact, differ significantly, the actual losses would be nonetheless the measure of the cost.

(5) LIMITATION ON SELF-INSURANCE CHARGE

The proposals which were published in the FEDERAL REGISTER provided that the self-insurance charge plus insurance administration expenses could be equal to, but could not exceed, the cost of comparable purchased insurance plus the associated administration expenses. Several respondents saw this as a question of allowability. It is, however, not a limit on allowability; it permits the cost of comparable purchased insurance to be used as one means of estimating the projected average loss. The provision is intended to avoid the necessity of employing actuaries to perform computations which other actuaries have already performed for the insurance company in setting the premium. The standard has been modified to express this intention more clearly.

Other respondents were concerned that a company which calculated a self-insurance charge based on, say, a 5-year moving average of its own loss experience would encounter problems if it were to incur a large loss; this would raise its average above the cost of comparable purchased insurance and thereby preclude the recovery of the excess over time. Again, the Board intended the limitation to apply only where the cost of comparable purchased insurance is used as a convenient method of estimating the projected average loss. The standard specifically requires that the contractor's own loss experience be reviewed regularly and that self-insurance charges for future periods reflect such experience in the same manner as would purchased insurance. It should be noted that the cost of future insurance premiums would also be expected to reflect, to some degree, the unfavorable loss experience of the contractor.

Several respondents were concerned that the standard would require them to obtain quotations for insurance premiums for comparison with proposed self-insurance charges, and they questioned the feasibility of obtaining such quotations. The standard only requires such a quotation if the self-insurance charge is to be estimated thereby; it would not be required if, for example, the charge were to be based only on a projection of the contractor's own experience.

(6) TERMINOLOGY

Several respondents suggested that, in the definition of "actual cash value," the phrase "replacement cost less depreciation" could lead to confusion because the type of depreciation intended thereby was not clear. The phrase was intended to imply replacement of the destroyed asset with one in the same physical condition. The definition has been modified to make this intention clearer.

One respondent suggested that the provisions of § 416.50(a)(1)(v) relative to "insurance coverage on retired lives" should be applicable to all types of insurance, rather than being limited to life insurance. The Board intended that this phrase provide for all types of insurance for retired persons. The term "retired lives" has accordingly been replaced by the term "retired persons."

Two respondents asked that the standard define or prescribe criteria for determining when a loss is considered to be "catastrophic" for purposes of home-office reinsurance agreements; they were concerned about after-the-fact disagreement as to whether a particular loss was "catastrophic" and thereby to be allocated in part to the home office, or "noncatastrophic" and to be absorbed entirely by the segment. The Board believes that what constitutes "catastrophic loss" depends on the individual circumstances of each contractor. The determination should be made at the time the internal loss-sharing policy is established and should be revised, as necessary, for changes in future circumstances. Obviously, a catastrophic loss would be one which would be very large in relation to the average loss per occurrence for that exposure, and losses of that magnitude would be expected to occur infrequently.

(7) PREMIUMS AND REFUNDS

The proposed standard provided that a premium refund or dividend would become an adjustment to the pro rata premium cost for the earliest cost accounting period in which the refund or dividend is actually or constructively received. However, the standard permitted the contractor the option of using estimated net premiums instead. One respondent suggested that the standard permit the shifting of adjustments to prior years for purposes of overhead analysis. This proposed change would not assure consistent measurement of cost; it has therefore not been adopted.

(8) DIRECT CHARGING OF PREMIUMS

Section 416.50(a)(1)(ii) provides that where insurance is purchased specifically for, and directly allocated to, a single final cost objective, the premiums need not be prorated. One respondent was concerned that if the final cost objective included requirements for two or more customers and the insurance premium were not prorated over the policy period, the cost might be charged only to the earliest units of production. They suggested that the provision be qualified by limiting it to only those final cost objectives which include requirements for a single customer. If the need for the insurance were to be occasioned by only one customer's requirements, the cost should be allocated to only that customer's units regardless of the production sequence. If the requirement is common to all customers' units, it should be allocated to all units.

The accounting principle here is the same as the one for specialized materials, which are charged directly to a final cost objective at the time of acquisition. If costs within a final cost objective, either for materials or for purchased insurance, were to be inappropriately related among the customers whose work is accumulated in the same cost objective, the problem would not be one of allocating costs to that cost objective. Rather it would be a problem of the method of analyzing costs within that final cost objective, a subject not being dealt with here.

(9) DEPOSITS AND RESERVES

Insurance agreements frequently provide for substantial amounts to be held by the insurer for various contingencies. Such amounts may be negotiated in advance or may represent the unrefunded excess of premiums over losses; in either event they are not arrived at by actuarial computations of known risks. The contractor typically retains a significant amount of interest in, and control over, such funds. FASB statement No. 5 provides that amounts which do not represent transfers of risk from the insured to the insurer are deposits and should be accounted for as such. The proposed standard required that anything which would be a deposit under that statement be treated as a deposit for contract costing purposes. In addition, the standard required that "reserves" held by the insurer for the account of the contractor would be regarded as deposits unless they met stated criteria.

These special criteria included a prohibition against recapture of the reserve or fund so long as any beneficiary remained alive. Two commentators urged that this test be modified. The Board intended to assure that the cost had indeed been incurred, but there was no intention to tie up excess reserves for long periods. The provision has been modified accordingly.

One respondent pointed out that group insurance carriers in recent years have required that premium stabilization reserves be established on medium-size experience-rated programs to smooth the experience so it will be similar to a large group. He said that the contractor has no more right to these reserves than the monthly premium he pays on the policy. He therefore suggested that the reserves required by the insurance carrier should not be required to be treated as deposits unless these reserves are treated as deposits for financial statement purposes. The Board does not agree; such reserves are negotiated amounts and the contractor does in fact have some influence over them. Cost measurement is improved if these amounts are treated as deposits until settled.

Some respondents previously pointed out that where a contractor changes from a pay-as-you-go program for retired persons to a pre-funded program, or initially establishes a pre-funded program, a liability arises to those employees who have already retired. The respondent suggested that the standard provide a transition mechanism to deal with the newly recognized liability. Therefore, the standard which was proposed in the May 15, 1978, FEDERAL REGISTER provided and the standard being promulgated today provides that, for a transition from a pay-as-you-go plan to a terminal-funded plan, or on the initial establishment of a terminal funded plan, the actuarial present value of benefits applicable to employees already retired shall be amortized over a period of 15 years.

Two respondents inquired as to the Board's reason for not providing a similar provision for transitions to fully prefunded level-premium or entry-age-normal plans. The actuarial premium computations for such plans implicitly allow for appropriate amortization of the liability for past service; therefore, an explicit provision for this purpose is unnecessary.

Two respondents asked for some liberalization of the 15-year amortization requirement; one suggested that the period be negotiable depending upon the circumstances which occasioned the change, as for example, when a segment is abolished and many employees take immediate retirement. The 15-year period was chosen to be comparable to the amortization period for actuarial gains and losses contained in CAS 413. To permit the amortization period to be negotiated on a case-by-case basis would reduce uniformity. It might also create an incentive to make such changes at times when one of the parties could be expected to benefit. The Board does not accept the suggestion.

(10) RELATIONSHIP TO OTHER STANDARDS

One respondent was concerned about the relationship of this standard to two other cost accounting standards, CAS No. 412, composition and measurement of pension cost, and CAS No. 415, accounting for costs of deferred compensation. The respondent was concerned especially about health insurance carried for retired employees of a contractor; he felt that there might be confusion as to whether such insurance should be considered a form of deferred compensation, a part of a pension plan, or a part of an insurance program.

The Board believes that these standards provide ample criteria for determining which standard is applicable to any given cost. In particular, the question of whether a benefit, such as insurance provided to retired persons, is an integral part of a pension plan and thereby governed by CAS No. 412 or is a part of an insurance program and thereby governed by CAS No. 416 is a question of fact in each given instance. Moreover, application of either standard to this element would result in substantially the same amounts of allocable cost.

(11) AMOUNT OF A LOSS

The proposal which was published in the October 5, 1977, FEDERAL REGISTER provided, in part, that "the amount of an incurred loss shall be measured by the net book value of property destroyed . . ." A number of respondents disagreed with this provision and suggested that the proper measure of the loss was "fair value," "replacement cost," "replacement cost, net of depreciation," and "replacement cost if replaced and net book value if not replaced." After considering these comments, the Board concluded that the measure of the loss should be the economic value of the asset destroyed, and that this value was best described as "actual cash value"; consequently, the May 15, 1978, FEDERAL REGISTER proposal incorporated "actual cash value."

Three respondents have again asked that the standard recognize replacement cost as the measure of the loss, on the grounds that the asset would probably be replaced with a new asset and that the cost of insurance premiums which would provide for replacement cost coverage would be allowable. The Board believes that the measure of the loss is the economic value of the asset destroyed, and this may bear little relationship to the economic value of the asset which is acquired to replace it. In this connection it should also be noted that CAS No. 409 requires the treatment of a gain on involuntary conversion of an asset as a recovery of past depreciation or, alternatively, treatment as a reduction in the cost basis of the replacement asset. The Board has, accordingly, retained the use of "actual cash value" as one of the major measures of loss.

Contract audit agencies have reported that contractors sometimes charge the maximum potential loss for contract costing purposes but report a lesser amount for published financial statements; therefore, the proposed standard provided that where the amount of the loss is uncertain, the estimate of the loss shall be the amount includible in published financial statements. Three respondents suggested that this requirement be deleted because the amount reported for financial statement purposes might be too conservative. The Board continues to believe that the guidance contained in FASB statement No. 5 and interpretation No. 14 thereto permits an objective measure of the loss. The Board, therefore, retains the requirement.

One respondent was concerned about whether use of the term "incurred loss" in § 416.50(a)(3) was intended to mean something other than an actual loss. The Board did not so intend; the term "incurred loss" has been eliminated.

Two respondents asked the Board to clarify the references to "publish financial statements" contained in the previously proposed standards. One of these respondents pointed out that not all published financial statements are necessarily prepared in accordance with generally accepted accounting principles; the other pointed out that a loss may be required to be reported in a published financial statement under conditions where it is not accruable therein as a liability. In order to clarify its intent, the Board has replaced the phrase "published financial statements," whenever it appeared in the proposed standard, with the phrase "statements prepared in accordance with generally accepted accounting principles" and the standard now refers to the amount which would be "includible as an accrued liability" in such statements.

(12) PRESENT VALUE OF FUTURE LOSSES

One respondent objected to the requirement for discounting amounts of losses to be paid in the future at a rate different from that contained in existing procurement regulations. As it stated in the prefatory remarks which accompanied the May 15, 1978, FEDERAL REGISTER publication, the Board believes that the additional computational effort involved in using a rate for contract costing different from that required by the various States is not warranted. Where no rate is prescribed by a State, the use of the rate determined by the Secretary of the Treasury pursuant to Pub. L. 92-41, 85 Stat. 97, as required by the standard, is consistent with the Board's requirement in CAS 415 to use that rate in discounting deferred compensation awards.

(13) ALLOCATION OF INSURANCE COSTS FROM A HOME OFFICE TO SEGMENTS

The October 5, 1977, proposal contained criteria for the allocation of insurance costs from a home office to segments. Various respondents questioned the need for such additional guidance on the grounds that the provisions of CAS 403 are adequate for this purpose. The Board concurred in this belief and omitted the related provisions from the May 15, 1978, proposal. Two respondents to that proposal suggested that the provisions of CAS 403 are too general and further guidance is needed to insure that such allocations will reflect significant differences in segment loss experience.

CAS 403 requires that home office expenses shall be allocated on the basis of the beneficial or casual relationship between supporting and receiving activities. Specifically, with respect to central payments or accruals made by a home office on behalf of its segments, CAS 403 requires that these shall be allocated directly to segments to the extent that they can be identified. CAS 403 provides further that payments or accruals which cannot be identified with individual segments are to be allocated by means of an allocation base representative of the factors on which the total payment is based. If there are significant differences in segment loss experience, then these differences would be identifiable and would be required by CAS 403 to be reflected in the allocation of the related home office premium cost or refund. The Board therefore continues to believe that additional guidance for such allocations in this standard is not necessary.

(14) MATERIALITY OF LOSSES AND INSURANCE ADMINISTRATION EXPENSES

The standard permits a contractor to recognize immaterial amounts of self-insured losses and insurance administration expenses as part of other expense categories rather than as "insurance expense." Two respondents were concerned that what is a "material" cost will be the subject of controversy.

The Board recognizes that some contractors may elect to purchase all of their insurance services from an insurance company or outside agencies; such services as claims processing or payment, risk analysis, loss prevention activities, etc. may be billed separately or included in the premium. Other contractors may elect to provide some or all of these serviecs themselves. The standard recognizes this diversity of practice by stating, in § 416.40, that the amount of the insurance cost is the sum of the projected average loss plus the insurance administration expenses.

Where a contractor purchases substantially all of its insurance services and the cost is included in the premium, the allocation of the costs of such services automatically follows the allocation of the premium. In such situations, if immaterial amounts of inhouse costs, such as portions of various individuals' salaries or allocable space costs, are not explicitly recognized as insurance administration expenses, the accuracy of cost allocation is not significantly impaired. On the other hand, if a contractor establishes a claim processing department to process group insurance claims for a large work force, and the costs of such a group are material, then the Board believes that uniformity will be better served by requiring that such costs be allocated in the same manner as the costs of the related insurance. The Board believes that its previous pronouncements on the subject of materiality will provide sufficient guidance.

(15) RENEGOTIATION

One respondent was concerned that contractors will have difficulty in following the standard while reporting to the Renegotiation Board, which is bound by law to allow items in accordance with chapter 1 of the Internal Revenue Code. This concern applies both to the election to account for refunds, dividends, and additional assessments on the basis of estimated net premiums, authorized in § 416.50(a)(1)(vi), and the use of a self-insurance charge in lieu of the recognition of actual losses. In both instances the standard could result in the recognition, as contract cost, of amounts which would not be recognized for tax purposes.

Other cost accounting standards have required the selection of specific cost measurement techniques from among the many which might have been available under the Internal Revenue Code. The respondent suggested that the proposal on insurance is different in that it can result in the use of a method of contract cost accounting which is not permitted for tax accounting purposes

The Board recognizes that the Renegotiation Board is indeed bound by law to recognize those elements of cost which are identified in the Internal Revenue Code. Measurement of the amounts of such costs to be recognized in any particular period, however, should be done in accordance with the best available accounting techniques. Where this standard recognizes a self-insurance charge in lieu of actual losses, the Renegotiation Board will also obtain a better measure of contractural profits by following the standard than by followng the tax measurement. The Renegotiation Board, as a relevant Federal agency, can arrange for the application of this standard as it has for various others which have required reconciliations between tax reporting and contract costing. No exemption is, therefore, being made for renegotiation.

(16) RECORDS

A contractor who elects to make a self-insurance charge should be expected to provide sufficient documentation to support the amount of the charge. In addition, the standard requires that the contractor's own loss experience be evaluated regularly. Finally, the standard requires the identification of losses to the segment in which they occur. While the cost of losses is already reflected in the contractor's formal accounting records, the data on loss frequency, amount, and location which may be necessary to comply with the proposed standard may not be a normal part of such accounting records. The "records" provision of the standard recognizes both the need for such data and the probable memorandum nature of the records. The requirement to maintain such records was contained in the October 5, 1977, proposal but was inadvertently omitted from the May 15, 1978, FEDERAL REGISTER proposal. It has been reinstated in the standard now being promulgated.

(17) ILLUSTRATIONS

One respondent suggested that the dollar amounts used in illustrations were unrealistic and would serve as guidelines for unrealistic rulings in practice. As the Board has stated on previous occasions, the use of dollar amounts in illustrations is intended to improve the understandability of the illustration. Such dollar amounts are not intended to establish criteria for use in actual situations.

(18) COSTS AND BENEFITS

The Board's objective, with respect to uniformity, is to achieve comparability among entities operating under like circumstances. As applied to the measurement of insurance costs, there should be similar reported costs where there are similar exposures to risk. The Board has recognized the need to provide guidance on the determination of contract charges under self-insurance programs, especially under circumstances where the likelihood is that actual losses in a given period will differ materially from the long-term projected average. This standard will provide for increased uniformity in this field.

Consistency pertains to the use, by any one entity, of cost accounting practices which permit comparability of contract results under similar circumstances over periods of time. The decision whether to purchase insurance or to self insure is comparable to a make or buy decision. A change in the method of providing for the risks (which risks continue unchanged) is not a change in circumstances of the sort which should destroy comparability over time. This standard provides the basis for consistency in measuring insurance costs even when there are shifts between purchased insurance and self-insurance.

Only three respondents suggested that the implementation costs of the standard would be excessive or would exceed the benefits. One of these foresaw increased administrative costs but did not offer any specifics. The concerns of the others appeared to lie primarily in two areas—the lack of a definition of "materiality" in relation to insurance costs and the lack of specific procedural guidance in estimating a self-insurance charge. They therefore anticipated increased disagreements. The board has provided remarks about materiality in various public pronouncements. The Board believes that these comments are sufficient and that the concerns in this regard are unwarranted.

A self-insurance charge is an estimate, and the Board has consistently refrained from dictating detailed estimating procedures. A contractor must, of necessity, estimate many costs, and the degree of sophistication and complexity of the estimating process is a matter for discussion between the contractor and procurement and audit personnel.

The standard provides for several methods of recognizing the costs of self-insurance. First, the contractor may recognize actual losses in those situations in which the distribution of actual losses may be expected to not differ significantly from the projected average loss. This is a matter which should be readily determinable from the nature of the exposure to risk; this will normally be expected where there are many units exposed to loss and the potential loss per unit is low in relation to the total exposure, as, for example, with worker's compensation, group insurance, and deductible portion of property and casualty insurance which is nominal in relation to the total exposure. In most such cases, contractors already charge actual losses, so no change will be necessary. Second, the contractor may use the premium cost of purchased insurance for comparable coverage as the basis for the self-insurance charge. This method would be appropriate when, for example, the contractor proposed to substantially increase a deductible provision for property and casualty insurance; he might propose to make a self-insurance charge equal to the premium reduction for the decreased coverage. Only in the event that either of these two methods is appropriate would the contractor have to resort to the third method, that of actuarial review of his own or industry experience to develop a self-insurance charge. Under these circumstances, the board believes that the majority of contractors will already be in compliance with the proposed standard and the costs of compliance for the remainder should not be significant. Therefore, the standard should have no significant inflationary impact.

Four respondents suggested that, if the majority of contractors would not have to change in order to comply with the standard, then the problems were not sufficient to justify the standard. The Board recognizes that, although the insurance problems resolved by this standard are likely to be encountered only by a minority of contractors, when they are encountered they are of substantial importance and their resolution in a uniform and consistent manner will be beneficial in contract costing.

In summary, the Board finds that this standard will increase the uniformity and consistency of measurement of the cost of insurance related to negotiated defense contracts. The standard will eliminate, or materially reduce, the problems listed in the Board's prefatory remarks with the May 15, 1978 publication. The Board finds that the costs of implementation will be slight and that there will be no inflationary impact.

* * * * *

There is also being published today an amendment to Part 400, definitions, to incorporate in that part terms defined in § 416.30(a) of this cost accounting standard.

PART 417—COST OF MONEY AS AN ELEMENT OF THE COST OF CAPITAL ASSETS UNDER CONSTRUCTION

Sec.
417.10 General applicability.
417.20 Purpose.
417.30 Definitions.
417.40 Fundamental requirement.
417.50 Techniques for application.
417.60 Illustrations.
417.70 Exemptions.
417.80 Effective date.
Preamble A

Authority: Sec. 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168).

Source: 45 FR 48574, July 21, 1980, unless otherwise noted.

Editorial Note: A supplement, consisting of the preamble to these regulations as they appeared in the Federal Register, follows the text of this part. This preamble is intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (45 FR 48573, July 21, 1980) is set forth in preamble A of the supplement.

§ 417.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (4 CFR 331.30).

§ 417.20 Purpose.

The purpose of this Cost Accounting Standard is to establish criteria for the measurement of the cost of money attributable to capital assets under construction, fabrication or development as an element of the cost of those assets. Consistent application of these criteria will improve cost measurement by providing for recognition of cost of contractor investment in assets under construction, and will provide greater uniformity in accounting for asset acquisition costs.

§ 417.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Intangible Capital Asset.* An asset that has no physical substance, has more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the benefits it yields.

(2) *Tangible Capital Assets.* An asset that has physical substance, more than minimal value, and is expected to be held by an enterprise for continued use or possession beyond the current accounting period for the services it yields.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 417.40 Fundamental requirement.

The cost of money applicable to the investment in tangible and intangible capital assets being constructed, fabricated or developed for a contractor's own use shall be included in the capitalized acquisition cost of such assets.

§ 417.50 Techniques for application.

(a) The cost of money for an asset shall be calculated as follows:

(1) The cost of money rate used shall be based on interest rates determined by the Secretary of the Treasury pursuant to Pub. L. 92-41 (85 Stat. 97).

(2) A representative investment amount shall be determined each cost accounting period for each capital asset being constructed, fabricated or developed giving appropriate consideration to the rate at which costs of construction are incurred.

(3) Other methods for calculating the cost of money to be capitalized, such as the method used for financial accounting and reporting, may be used, provided the resulting amount does not differ materially from the amount calculated by use of paragraphs (a) (1) and (2), of this section.

(b) If substantially all the activities necessary to get the asset ready for its intended use are discontinued, cost of money shall not be capitalized for the period of discontinuance. However, if such discontinuance arises out of causes beyond the control and without the fault or negligence of the contractor, cessation of cost of money capitalization is not required.

§ 417.60 Illustrations.

(a) A contractor decided to build a major addition to his plant using both his own labor and outside subcontractors. It took 13 months to complete the building. The first 10 months of the construction period were in one cost accounting period. At the end of the cost accounting period the total charges, including cost of money computed in accordance with 4 CFR Part 414, accumulated in the construction-in-progress account for this project amounted to $750,000. However, most of these construction costs were incurred towards the end of the cost accounting period. In developing a method for determining a representative investment amount appropriate consideration must be given to the rate at which costs have been incurred in accordance with § 417.50(a)(ii). Therefore, the contractor averaged the 10 month-end balances and determined that the average investment in the project was $245,000. Two cost of money rates were in effect during the 10-month period; their time-weighted average was determined to be 8.6%. Application of the 8.6% rate for $^{10}/_{12}$ of a year to the representative balance of $245,000 resulted in the determination that $17,448 should be added to the construction-in-progress account in recognition of the cost of money related to this project in its first cost accounting period. The project was completed with the addition of $750,000 of additional costs during the first three months of the subsequent cost accounting period. The contractor considered the three month-end balances (which included the $17,558 capitalized cost of money described in the preceding paragraph) and determined that the representative balance was $1,234,000. The cost of money rate in effect during this three-month period was 7.75%. Applying the rate of 7.75% for ¼ of a year to the balance of $1,234,000 resulted in a determination that $23,909 should be added to the construction-in-progress account in recognition of the cost of money while under construction in the second cost accounting period. The capitalized project was put into service at the recognized cost of acquisition of $1,541,467 which consists of the "regular" costs of $1,500,000 plus $17,558 and $23,909 cost of money. This practice is in accordance with § 417.50(a) and other applicable provisions of the Standard.

NOTE: An alternative technique would be to make separate calculations, using an appropriate investment amount and cost of money rate, for each month. The sum of the monthly cost of money amounts could be entered in the construction-in-progress account once each cost accounting period.

(b) A contractor built a major addition with identical basic data to those described in § 417.60(a) except that the costs were incurred at a fairly uniform rate throughout the period. Because of the pattern of cost incurrence the contractor used beginning and ending balances of the cost accounting period to find the representative amounts. For the first cost accounting period the representative investment amount was the average of the beginning and ending balances (zero and $750,000), or $375,000. Application of the average interest rate of 8.6% for $^{10}/_{12}$ of a year resulted in the determination that $26,875 should be added to the construction-in-progress account in recognition of the cost of money related to this project in its first cost accounting period. During the subsequent three months the contractor used the representative balance of $1,151,875, derived by averaging the beginning balance of $776,875 ($750,000 "regular" cost plus the $26,875 imputed cost from the prior period) and the balance at the end, $1,526,875. Applying the 7.75% cost of money rate to this balance for a three-month period resulted in a determination that $22,317 should be added to the construction-in-progress account in recognition of the cost of money while under construction in the second cost accounting period. The capitalized project was put into service at the recognized cost of acquisition of $1,549,192 which consists of the "regular" costs of $1,500,000 plus $26,875 and $22,317 imputed cost of money. This practice is in accordance with § 417.50(a) and other applicable provisions of the Standard.

NOTE: If this contractor, acting in accordance with established Standards for financial accounting, allocated a portion of its paid interest expense to this construction project and the resultant acquisition cost for financial reporting purposes was not materially different from $1,549,192, the contractor could, in accordance with § 417.50(a)(iii), use the same acquisition cost for contract costing purposes.

§ 417.70 Exemptions.

None for this Standard.

§ 417.80 Effective date.

(a) The effective date of this Cost Accounting Standard is December 15, 1980.

(b) This Cost Accounting Standard shall be followed by each contractor on or after the start of his next cost accounting period beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

PREAMBLE A

Preamble to Original Publication, 7-21-80

The following is the preamble to the original publication of Part 417, 45 FR 48574, July 21, 1980.

SUMMARY

The Cost Accounting Standards Board is Promulgating Cost Accounting Standard No. 417, one of the series of Standards being issued pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168).

This Standard provides for the determination of an imputed cost of money to be included in the capitalized cost of acquisition of assets developed, fabricated or constructed for a contractor's own use. Application of this Standard will provide increased uniformity in accounting for the acquisition costs of assets.

EFFECTIVE DATE

December 15, 1980.

SUPPLEMENTARY INFORMATION

(1) BACKGROUND

Cost Accounting Standard (CAS) 417 being promulgated today is based on the same concept as CAS 414, which provides criteria for the measurement and allocation of the cost of money as a part of the cost of tangible and intangible capital assets. CAS 417 provides guidance for the measurement of the cost of money as an element of the cost of capital assets under construction. A proposed Standard on this topic, designated CAS 421, was published in the FEDERAL REGISTER on January 4, 1980. The Board received 36 letters of comment on that proposal and takes this opportunity to express its appreciation for the many helpful suggestions and constructive criticisms that were received.

(2) NEED FOR A STANDARD

Most commentators favored the January 1980 proposal. Those who opposed it did so on the basis that they did not favor Standard No. 414 and do not favor any extension of the principle of that Standard. The Board, in promulgating CAS 414, provided for an important element of contract cost, that of the cost of money related to investment in facilities used in contract performance. Contractor investments committed to facilities not yet in service involve a similar economic cost.

The Board believes that this Standard is an appropriate extension of the concept.

(3) PROPOSALS TO AMEND CAS 414

A number of contractors suggested that instead of capitalizing cost of money, it should be treated as a current cost and therefore an amendment should be made to CAS 414 to recognize this cost on current contracts. The Board believes that capitalization of cost of money, in contrast to the immediate recognition of cost of money as a contract cost, will place such costs on the same basis as other construction costs and thus provide for the total cost of new assets to be charged to output of the periods when they are used in the production of goods and services.

(4) CAPITALIZATION OF PAID INTEREST

The proposed Standard No. 421 provided an option to capitalize either cost of money computed in accordance with the provisions of the Standard or the amount capitalized for financial accounting and reporting purposes pursuant to FAS No. 34. This option was offered in order to simplify the record-keeping procedures as it would have enabled the contractor to avoid a duplicate set of records—one for financial accounting and the other for Government contract costing purposes.

A number of Government agencies disagreed with this approach. It was pointed out that no true compatibility exists between FAS No. 34 and the proposed CAS 421 since the former specifically prohibits recognition of any type of imputed interest cost for capitalization purposes. It was also stated that the option to elect between the two methods of capitalization in the proposed CAS 421 would lead to inconsistent capitalization practices among contractors. Furthermore, it was pointed out that paid interest is an unallowable cost under pertinent procurement regulations. One major agency pointed out that if the Standard were to allow the choice as proposed, any contractor making the election to capitalize interest actually paid "* * * will have such costs disallowed when included in depreciation subsequently claimed as a cost under Government contracts." Such disallowance would effectively nullify the option.

In view of these comments by Government procurement agencies the Board has concluded that it would be futile at this time to proceed with the unrestricted option that permits capitalization of the amount capitalized for financial accounting and reporting purposes. The Standard, as promulgated, permits only capitalization of cost of money computed in accordance with the provisions of this Standard, or the amount used for financial reporting where it is not a materially different amount.

(5) ONE-YEAR LIMITATION

The proposed Standard required that in order to capitalize cost of money the construction or fabrication effort must be sustained at least for one year. This provision was based on the belief that administrative costs would typically be higher than the benefits to be expected from capitalization of cost of money for minor projects. Numerous commentators pointed out that irrespective of any administrative costs the cost of money could be quite material on a project lasting less than a year. The Board agrees with this view and has eliminated the restriction on the length of the construction period. The Board expects that contractors will apply the Standard where the benefits to be derived from improved cost measurement and allocation can be expected to outweigh the costs of implementation.

(6) COMPUTATION OF THE "REPRESENTATIVE INVESTMENT AMOUNT"

Some commentators questioned whether there are any constraints imposed on the methods that may be used for determining the "representative investment amount." The Standard specifies in § 417.50(a)(ii) [previously designated as § 421.50(e)] only that the method selected should give appropriate consideration to the "rate at which costs of construction are incurred."

The wording in illustrations § 417.60 (a) and (b) has been changed to demonstrate more clearly when the use of beginning and ending balances of a cost accounting period is appropriate. If major fluctuations are expected in the rate of cost incurrence, averaging of balances for shorter time periods, such as months, is appropriate.

(7) APPLICABILITY

The proposed Standard was to be applied only to those assets on which construction began after the Standard became applicable. Several commentators pointed out the desirability of immediate application with respect to all assets under construction.

The wording in § 417.80 has been changed to extend the coverage to all the assets under construction at the time when the Standard is first applied by the contractor.

(8) COSTS AND BENEFITS

The Board recognizes that there are economic costs related to a contractor's investment in the construction period for assets subject to this Standard. The cost, even though imputed, is real and is relevant for the contract costing. It has heretofore not been a part of contract costing. This Standard provides for its measurement and therefore will improve the quality of cost ascertainment on contracts where the assets are used.

Limitation on the option to use, for contract costing, the amounts capitalized under FAS 34 may impose certain administrative costs for some contractors. The Board is persuaded that these costs, in general, will not be significant, and they are surely outweighed by the benefit of more consistent contract cost measurement which will be derived from the operation of this Standard.

Title 4 CFR Chapter III is amended by adding a new Part 417 to read as follows:

PART 418—ALLOCATION OF DIRECT AND INDIRECT COSTS

Sec.
418.10 General applicability.
418.20 Purpose.
418.30 Definitions.
418.40 Fundamental requirements.
418.50 Techniques for application.
418.60 Illustrations.
418.70 Exemptions.
418.80 Effective date.
PREAMBLE A

AUTHORITY: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

SOURCE: 45 FR 31932, May 15, 1980, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble is intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (45 FR 31929, May 15, 1980) is set forth in preamble A of the supplement.

§ 418.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirements to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts (4 CFR 331.30).

§ 418.20 Purpose.

The purpose of this Cost Accounting Standard is (a) to provide for consistent determination of direct and indirect costs, (b) to provide criteria for the accumulation of indirect costs, including service center and overhead costs, in indirect cost pools, and (c) to provide guidance relating to the selection of allocation measures based on the beneficial or causal relationship between an indirect cost pool and cost objectives. Consistent application of these criteria and guidance will improve classification of costs as direct and indirect and the allocation of indirect costs.

§ 418.30 Definitions.

(a) The following are definitions of terms prominent in this Standard.

(1) *Allocate.* To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Direct cost.* Any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or

labor. Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives.

(3) *Indirect cost.* Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(4) *Indirect cost pool.* A grouping of incurred costs identified with two or more cost objectives but not identified specifically with any final cost objective.

(b) The following modifications of definitions set fourth in Part 400 of this chapter are applicable to this Standard: None.

§ 418.40 Fundamental requirements.

(a) A business unit shall have a written statement of accounting policies and practices for classifying costs as direct or indirect which shall be consistently applied.

(b) Indirect costs shall be accumulated in indirect cost pools which are homogeneous.

(c) Pooled costs shall be allocated to cost objectives in reasonable proportion to the beneficial or causal relationship of the pooled costs to cost objectives as follows:

(1) If a material amount of the costs included in a cost pool are costs of management or supervision of activities involving direct labor or direct material costs, resource consumption cannot be specifically identified with cost objectives. In that circumstance, a base shall be used which is representative of the activity being managed or supervised.

(2) If the cost pool does not contain a material amount of the costs of management or supervision of activities involving direct labor or direct material costs, resource consumption can be specifically identified with cost objectives. The pooled cost shall be allocated based on the specific identifiability of resource consumption with cost objectives by means of one of the following allocation bases:

(i) A resource consumption measure, (ii) an output measure, or (iii) a surrogate that is representative of resources consumed. The base shall be selected in accordance with the criteria set out in § 418.50(e).

(d) To the extent that any cost allocations are required by the provisions of other Cost Accounting Standards, such allocations are not subject to the provisions of this Standard.

(e) This Standard does not cover accounting for the costs of special facilities where such costs are accounted for in separate indirect cost pools.

§ 418.50 Techniques for application.

(a) *Determination of direct cost and indirect cost.* (1) The business unit's written policy classifying costs as direct or indirect shall be in conformity with the requirements of this Standard.

(2) In accounting for direct costs a business unit shall use actual costs, except that:

(i) Standard costs for material and labor may be used as provided in 4 CFR Part 407, or

(ii) An average cost or pre-established rate for labor may be used provided that (A) the functions performed are not materially disparate and employees involved are interchangeable with respect to the functions performed, or (B) the functions performed are materially disparate but the employees involved either all work in a single production unit yielding homogeneous outputs, or perform their respective functions as an integral team.

Whenever average cost or pre-established rates for labor are used, the variances, if material, shall be disposed of at least annually by allocation to cost objectives in proportion to the costs previously allocated to these cost objectives.

(3) Labor or material costs identified specifically with one of the particular cost objectives listed in paragraph (d)(3) of this section shall be accounted for as direct labor or direct material costs.

(b) *Homogeneous indirect cost pools.* (1) An indirect cost pool is homogeneous if each significant activity whose costs are included therein has the same or a similar beneficial or casual relationship to cost objectives as the other activities whose costs are included in the cost pool. It is also homogeneous if the allocation of the costs of the activities included in the cost pool result in an allocation to cost objectives which is not materially different from the allocation that would result if the costs of the activities were allocated separately.

(2) An indirect cost pool is not homogeneous if the costs of all significant activities in the cost pool do not have the same or a similar beneficial or causal relationship to cost objectives and, if the costs were allocated separately, the resulting allocation would be materially different. The determination of materiality shall be made using the criteria provided in 4 CFR 331.71.

(3) A homogeneous indirect cost pool shall include all indirect costs identified with the activity to which the pool relates.

(c) *Change in Allocation Base.* No change in an existing indirect cost pool allocation base is required if the allocation resulting from the existing base does not differ materially from the allocation that results from the use of the base determined to be most appropriate in accordance with the criteria set forth in paragraphs (d) and (e) of this section. The determination of materiality shall be made using the criteria provided in 4 CFR 331.71.

(d) *Allocation measures for an indirect cost pool which includes a material amount of the costs of management or supervision of activities involving direct labor or direct material costs.* (1) The costs of the management or supervision of activities involving direct labor or direct material costs do not have a direct and definitive relationship to the benefiting cost objectives and cannot be allocated on measures of a specific beneficial or causal relationship. In that circumstance, the base selected to measure the allocation of the pooled costs to cost objectives shall be a base representative of the activity being managed or supervised.

(2) The base used to represent the activity being managed or supervised shall be determined by the application of the criteria below. All significant elements of the selected base shall be included.

(i) A direct labor hour base or direct labor cost base shall be used, whichever in the aggregate is more likely to vary in proportion to the costs included in the cost pool being allocated, except that

(ii) A machine-hour base is appropriate if the costs in the cost pool are comprised predominantly of facility-related costs, such as depreciation, maintenance, and utilities, or

(iii) A units-of-production base is appropriate if there is common production of comparable units, or

(iv) A material cost base is appropriate if the activity being managed or supervised is a material-related activity.

(3) Indirect cost pools which include material amounts of the costs of management or supervision of activities involving direct labor or direct material costs shall be allocated to:

(i) Final cost objectives;

(ii) Goods produced for stock or product inventory;

(iii) Independent research and development and bid and proposal projects;

(iv) Cost centers used to accumulate costs identified with a process cost system (i.e., process cost centers);

(v) Goods or services produced or acquired for other segments of the contractor and for other cost objectives of a business unit; and

(vi) Self-construction, fabrication, betterment, improvement, or installation of tangible capital assets.

(e) *Allocation measures for indirect cost pools that do not include material amounts of the costs of management or supervision of activities involving direct labor or direct material costs.* Homogeneous indirect cost pools of this type have a direct and definitive relationship between the activities in the pool and benefiting cost objectives. The pooled costs shall be allocated using an appropriate measure of resource consumption. This determination shall be made in accordance with the following criteria taking into consideration the individual circumstances:

(1) The best representation of the beneficial or causal relationship between an indirect cost pool and the benefiting cost objectives is a measure

of resource consumption of the activities of the indirect cost pool.

(2) (i) If consumption measures are unavailable or impractical to ascertain, the next best representation of the beneficial or causal relationship for allocation is a measure of the output of the activities of the indirect cost pool. Thus, the output is substituted for a direct measure of the consumption of resources.

(ii) The use of the basic unit of output will not reflect the proportional consumption of resources in circumstances in which the level of resource consumption varies among the units of output produced. Where a material difference will result, either the output measure shall be modified or more than one output measure shall be used to reflect the resources consumed to perform the activity.

(3) If neither resources consumed nor output of the activities can be measured practically, a surrogate that varies in proportion to the services received shall be used to measure the resources consumed. Generally, such surrogates measure the activity of the cost objectives receiving the service.

(4) Allocation of indirect cost pools which benefit one another may be accomplished by use of (i) the cross-allocation (reciprocal) method, (ii) the sequential method, or (iii) another method the results of which approximate those achieved by either of the methods in paragraph (e)(4)(i) or paragraph (e)(4)(ii) of this section.

(5) Where the activities represented by an indirect cost pool provide services to two or more cost objectives simultaneously, the cost of such services shall be prorated between or among the cost objectives in reasonable proportion to the beneficial or causal relationship between the services and the cost objectives.

(f) *Special allocation.* Where a particular cost objective in relation to other cost objectives receives significantly more or less benefit from an indirect cost pool than would be reflected by the allocation of such costs using a base determined pursuant to paragraphs (d) and (e) of this section, the Government and contractor may agree to a special allocation from that indirect cost pool to the particular cost objective commensurate with the benefits received. The amount of a special allocation to any such cost objective made pursuant to such an agreement shall be excluded from the indirect cost pool and the particular cost objective's allocation base data shall be excluded from the base used to allocate the pool.

(g) *Use of pre-established rates for indirect costs.* (1) Pre-established rates, based on either forecasted actual or standard cost, may be used in allocating an indirect cost pool.

(2) Pre-established rates shall reflect the costs and activities anticipated for the cost accounting period except as provided in paragraph (g)(3) of this section. Such pre-established rates shall be reviewed at least annually, and revised as necessary to reflect the anticipated conditions.

(3) The contracting parties may agree on pre-established rates which are not based on costs and activities anticipated for a cost accounting period. The contractor shall have and consistently apply written policies for the establishment of these rates.

(4) Under paragraphs (g)(2) and (3) of this section where variances of a cost accounting period are material, these variances shall be disposed of by allocating them to cost objectives in proportion to the costs previously allocated to these cost objectives by use of the pre-established rates.

(5) If pre-established rates are revised during a cost accounting period and if the variances accumulated to the time of the revision are significant, the costs allocated to that time shall be adjusted to the amounts which would have been allocated using the revised pre-established rates.

§ 418.60 Illustrations.

(a) Business Unit A has various classifications of engineers whose time is spent in working directly on the production of the goods or services called for by contracts and other final cost objectives. In keeping with its written policy, detailed time records are kept of the hours worked by these engineers, showing the job/account numbers representing various cost objectives. On the basis of these detailed time records, Business Unit A allocates the labor costs of these engineers as direct labor costs of final cost objectives. This practice is in accordance with the requirements of § 418.50(a)(1).

(b) Business Unit B has a fabrication department, employees of which perform various functions on units of the work-in-process of multiple final cost objectives. These employees are grouped by labor skills and are interchangeable within the skill grouping. The average wage rate for each group is multiplied by the hours worked on each cost objective by employees in that group. The contractor classifies these costs as direct labor costs of each final cost objective. This cost accounting treatment is in accordance with the provisions of § 418.50(a)(2)(B)(i).

(c) Business Unit C accumulates the costs relating to building ownership, maintenance, and utility into one indirect cost pool designated "Occupancy Costs" for allocation to cost objectives. Each of these activities has the same or a similar beneficial or causal relationship to the cost objectives occupying a space. Business Unit C's practice is in conformance with the provisions of § 418.50(b)(1).

(d) Business Unit D includes the indirect costs of machining and assembling activities in a single manufacturing overhead pool. The machining activity does not have the same or similar beneficial or causal relationship to cost objectives as the assembling activity. Also, the allocation of the cost of the machining activity to cost objectives would be significantly different if allocated separately from the costs of the assembling activity. Business Unit D's single manufacturing overhead pool is not homogeneous in accordance with the provisions of § 413.50(b), and separate pools must be established in accordance with § 418.40(b).

(e) In accordance with § 418.50(b)(3), Business Unit E includes all the cost of occupancy in an indirect cost pool. In selecting an allocation measure for this indirect cost pool, the contractor establishes that it is impractical to ascertain a measurement of the consumption of resources in relation to the use of facilities by individual cost objectives. An output base, the number of square feet of space provided to users, can be measured practically; however, the cost to provide facilities is significantly different for various types of facilities such as warehouse, factory, and office and each type of facility requires a different level of resource consumption to provide the same number of square feet of usable space. Allocation on a basic unit measure of square feet of space occupied will not adequately reflect the proportional consumption of resources. Business Unit E establishes a weighted square foot measure for allocating occupancy costs, which reflects the different levels of resource consumption required to provide the different types of facilities. This practice is in conformance with provisions of § 418.50(e)(2)(B).

(f) Business Unit F has an indirect cost pool containing a significant amount of material-related costs. The contractor allocates these costs between his machining overhead cost pool and his assembly overhead cost pool. The business unit finds it impractical to use an allocation measure based on either consumption or output. The business unit selects a dollars of material-issued base which varies in proportion to the services rendered. The dollars of material-issued base is a surrogate base which conforms to the provisions of § 418.50(e)(3).

(g) Business Unit G has a machining activity for which it develops a separate overhead rate, using direct labor cost as the allocation base. The machining activity occasionally does significant amounts of work for other activities of the business unit. The labor used in doing the work for other activities is of the same nature as that used for contract work. However, the machining labor for other activities is not included in the base used to allocate the overhead costs of the machining activity. This practice is not in conformance with § 418.50(d)(2). Business Unit G must include the cost of labor doing work for the other activities in the allocation base for the machining activity indirect cost pool.

(h) Business Unit H accounts for the costs of company aircraft in a separate homogeneous indirect cost pool and allocates the cost to benefiting cost objectives using flight hours. Business Unit H prorates the cost of a single flight between benefiting cost objectives whenever simulataneous services have been rendered. Manager of Contract 2 learns of the trip and goes along with Manager of Contract 1. Business Unit H prorates the cost of the trip between Contract 1 and Contract 2. This practice is in conformance with the provision of § 418.50(e)(5).

(i) During a cost accounting period Business Unit I allocates the cost of its flight services indirect cost pool to other indirect cost pools and final cost objectives using a pre-established rate. The pre-established rate is based on an estimate of the actual costs and activity for the cost accounting period. For the cost accounting period Business Unit I establishes a rate of $200 per hour for use of the flight services activity. In March the contractor's operating environment changes significantly; the contractor now expects a significant increase in the cost of this activity during the remainder of the year. Business Unit I estimates the rate for the entire cost accounting period to be $240 an hour. Pursuant to the provisions of § 418.50(g)(4), the Business Unit may revise its rate to the expected $240 an hour. If the accumulated variances are significant, the business unit must also adjust the costs previously allocated to reflect the revised rates.

§ 418.70 Exemptions.

This standard shall not apply to contractors who are subject to the provisions of Federal Management Circular 74-4 (Principles for Determining Costs Applicable to Grants and Contracts with State and Local Governments).

§ 418.80 Effective date.

(a) The effective date of this Cost Accounting Standard is September 20, 1980.

(b) This Cost Accounting Standard shall be followed by each contractor on or after the start of his second fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

PREAMBLE A

Preamble to Original Publication, 5-15-80

The following is the preamble to the original publication of Part 418, 45 FR 31932, May 15, 1980.

SUMMARY

The Cost Accounting Standards Board is promulgating today Cost Accounting Standard (CAS) 418, Allocation of Direct and Indirect Costs. It is one of a series of Standards the Board is issuing pursuant to Section 719 of the Defense Production Act of 1950, as amended (Pub. L. 91-379, 50 U.S.C. App. 2168).

CAS 418 requires that costs be consistently classified as direct or indirect, establishes criteria for accumulating indirect costs in indirect cost pools, and sets forth guidance on allocating indirect cost pools. These topics are central to the Board's mission to issue Standards to achieve uniformity and consistency in the cost accounting practices followed by defense contractors in estimating, accumulating and reporting costs of defense contracts.

EFFECTIVE DATE

September 20, 1980.

SUPPLEMENTARY INFORMATION:

(1) BACKGROUND

The present Standard stems from two proposals, published in the FEDERAL REGISTER on March 16, 1978 and July 23, 1979.

The March 16, 1978 publication consisted of five proposed Standards:

- CAS 417—Distinguishing Between Direct and Indirect Costs.
- CAS 418—Allocation of Service Center Costs.
- CAS 419—Allocation of Material-Related Overhead Costs.
- CAS 420—Allocation of Manufacturing, Engineering and Comparable Overhead Costs.
- CAS 421—Allocation of Indirect Costs.

The Board received letters from 86 commentators on the March 16, 1978 publication. As a result of the comments and additional research performed at 10 contractor locations, the number of proposed Standards was reduced to three in the July 23, 1979 publication:

- CAS 417—Distinguishing Between Direct and Indirect Costs. (Continued as a separate Standard.)
- CAS 418—Allocation of Indirect Cost Pools. (Consolidated original CAS 418 and original CAS 421.)
- CAS 419—Allocation of Overhead Costs of Productive Functions and Productive Activities. (Consolidated original CAS 419 and original CAS 420.)

The Board received comments from 59 interested parties in response to the July 23, 1979 publication. In addition, representatives of three industry associations supplemented their views orally. After consideration of all views, the Board has determined that it is appropriate to reduce the degree of specificity contained in the July 23, 1979 publication. As a consequence, the Board has been able to consolidate the three proposed Standards into the one Standard being promulgated today.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

The following sections of these prefatory comments present the Board's views on the major issues raised by the commentators in response to the July 23, 1979 publication, and explains how these views are expressed in the current Standard.

(2) POTENTIAL IMPACT ON CONTRACTOR ACCOUNTING SYSTEMS

Based on staff research and the comments received on prior proposals, the Board recognizes that this Standard may have a pervasive impact on contractor accounting systems. Because of this, the Board here and in the Standard is emphasizing the necessity to evaluate any perceived need for change in cost accounting practices in terms of materiality. The need to evaluate the materiality of a change in cost accounting practice applies to all provisions of the Standard. It is not limited to those particular provisions of the Standard in which materiality is mentioned for emphasis.

In resolving questions of materiality, the Board refers the parties to the criteria found in 4 CFR 331.71. These criteria take into consideration a variety of factors including the absolute dollar amount of costs involved, whether the costs are direct or indirect, the relationship of the costs to a particular contract, and the impact on Government funding. The Board is persuaded by the comments received on prior proposals that the use of these criteria will lead to an appropriate implementation of this Standard.

Some commentators urged the Board to define materiality in terms of the net effect on the cost of the totality of Government contracts in relation to the costs of implementing any accounting change pursuant to the Standard. The Board's materiality criteria recognize the need to consider the impact of cost accounting changes on the costs of individual contracts. To reduce the probable impact on the number of pools or changes in allocation bases required under the Standard however, the Board urges the parties to give special consideration to the net effect without ignoring any of the criteria specified in § 331.71(a). The Board notes that a change which has the same directional impact on most Government contracts will be more material than one in which the directional impacts on the costs of various Government contracts are mixed.

Commentators were particularly concerned that the proposed Standards would require them to establish separate indirect cost pools or the change their allocation bases even where the allocation results would be substantially the same. The Board intends that the creation of additional indirect cost pools or change of allocation base will be required only if the changes will result in materially different allocations of cost.

In those circumstances in which a change in cost accounting practice is not required because of the present immateriality of impact, the Board notes that the impact may become material if circumstances should change. In this case acceptance of the existing system based on the immateriality of the impact would no longer pertain and the other criteria in the Standard would be applied to determine the appropriate accounting in the changed circumstances.

(3) DEFINITION OF DIRECT COST

The Standard being promulgated today includes the Board's definition of direct cost (§ 418.30(a)(2)). The Board originally issued the definition in 1972 as part of CAS 402, Consistency in Allocating Costs Incurred for the Same Purpose. Direct cost is defined as "any cost which is specifically identified with a particular final cost objective."

Commentators have criticized the definition on conceptual grounds and on the basis that it is contrary to common understanding of the term. They contend that a proper approach would recognize that all cost objectives have direct costs. Despite these criticisms, they indicate that no practical problems have resulted from the present definition.

The definition in CAS 402 was needed because of the type of consistency the Board requires in that Standard; that is, consistency in the allocation of direct and indirect costs with respect to final cost objectives. To broaden the definition of direct cost to say that all cost objectives have direct costs, would require a substantial change in CAS 402 in order to continue to achieve the purposes of that Standard.

Furthermore, the existing definition of direct cost facilitates description of allocation bases for the purposes of the Standard being promulgated today, as well as for other Standards. A change in the definition of direct costs as recommended by the commentators would necessitate a series of new definitions or lengthy descriptions of the types of direct cost which may be used for making up bases for allocating various indirect cost pools.

The Board believes that the present definition of direct cost serves useful purposes and has not created any problems. The Board, therefore, has decided to retain the present definition.

(4) NEED FOR WRITTEN POLICIES

The purpose of proposed Standard 417 was to distinguish between direct and indirect costs. Criteria were established for direct costs. Generally, costs not meeting those criteria were to be classified as indirect.

Many commentators objected to the proposed Standard. They claimed that the criteria were too restrictive and would have required the reclassification from direct to indirect of many costs that have a close relationship to final cost objectives.

The Board has considered the statements made by the commentators and has studied other information it has developed. The Board has concluded that more flexibility should be allowed concerning the classification of costs as direct than was permitted by proposed CAS 417. That proposed Standard has been eliminated, and a requirement has been added to CAS 418 (§§ 418.40(a) and 418.50(a)(1)) for a written statement, in which each contractor must set forth his policies and practices for classifying costs as direct or indirect. The degree of detail that the statement should contain is a matter for decision by the contracting parties.

(5) AVERAGE AND PRE-ESTABLISHED DIRECT LABOR RATES

Proposed CAS 417 provided in § 417.50(b) that: "The amount of cost to be allocated as a direct cost to final cost objectives may be determined on the basis of an average cost of the resources used or applied whenever the resources are interchangeable." Several commentators believe that the requirement that resources be "interchangeable" before their costs could be averaged was too strict. They said that "interchangeable" would be interpreted to mean "identical." The principal concern was with average and pre-established direct labor rates. The commentators said that few labor resources are identical or even "productively interchangeable," and that consequently the interchangeability criterion would cause the creation of many more labor rates.

The Board believes there is no conceptual difference between average and pre-established direct labor rates and labor-rate standards, which are governed by CAS 407. Use of Standard Costs for Direct Material and Direct Labor. Retention of interchangeability as the sole criterion for average and pre-established direct labor rates would impose stricter criteria for those rates than CAS 407 imposes for labor-rate standards. Accordingly, the Board decided to apply the same criteria to average and pre-established direct labor rates that are used in CAS 407 for labor-rate standards. The Standard now permits (§ 418.50(a)(2)(B)) two kinds of groupings in addition to those based on the principle of interchangeability. Average or pre-established direct labor rates may be set for a group of employees who (i) are interchangeable with respect to functions performed, (ii) produce homogeneous output, or (iii) form an integral team. The Board believes that these changes will avoid the problems foreseen by the commentators, and will be consistent with CAS 407.

(6) BLANKET COSTS

Blanket costs are labor or material costs accumulated in intermediate cost objectives and reallocated to final cost objectives as direct costs. Many commentators objected to § 417.50(c) of the proposed CAS 417, which would have permitted such costs to be classified as direct only if they were allocated from an intermediate cost objective by a measure of resource consumption or a measure of output. Commentators said that this was too restrictive. They claimed that, since most bases used to distribute blanket costs are surrogates for rather than direct measures of resource consumption, proposed CAS 417 would have required most blanket costs to be classified as indirect costs.

The Board has considered the statements made by the commentators and has removed the requirement that blanket costs in order to be classified as direct costs be allocated on the basis of direct measures of consumption or output.

(7) 5 PERCENT MATERIALITY TEST

A number of commentators expressed concern that the requirements of the proposed CAS 418 and 419 would lead to unnecessary proliferation of indirect cost pools. The proposed Standards would have required that a separate pool be created only where a material difference in cost allocation would result. The Board had proposed a 5 percent materiality test for this purpose. This provision drew a large number of responses. Most commentators expressed serious reservations about the practicality of such a test.

The 5 percent materiality test was included in the proposed CAS 419 for the express purpose of alleviating the concern expressed by many commentators about unnecessary proliferation of overhead pools. Many of the same commentators suggested that rather than specifying an arbitrary percentage, the Standard should rely on the materiality provision already included in the Board's rules and regulations. The Standard being promulgated today refers to § 331.71 which sets forth the materiality criteria for use in the application of all Standards.

(8) HOMOGENEOUS INDIRECT COST POOLS

Some commentators stated that the requirement of the proposed § 418.50(a)(1) for a homogeneous indirect cost pool could result in unnecessary proliferation of indirect cost pools. A number of commentators also characterized the requirements of the proposed § 418.50(a)(2) as being redundant or in conflict with the requirements of the proposed § 418.50(a)(1). The Board has revised the proposed § 418.50(a)(2) to parallel the language in proposed § 418.50(a)(1) to preclude any conflict between the two paragraphs. The Board continues to believe that the requirement for homogeneous pools based on the concept of beneficial or causal relationship is essential. The Board has emphasized in the revised § 418.50(b)(2) that a pool also is deemed to be homogeneous if the separate allocation of the costs of the dissimilar activities would not result in material differences. The Board has provided reference to its guidance on materiality contained in § 331.71.

Some commentators stated that the proposed § 418.50(a)(3), which dealt with dissimilar use of resources, was too detailed a prescription and as such would lead to unnecessary proliferation of indirect cost pools. The Board was persuaded that the coverage of this level of detail is not necessary in the single revised Standard and accordingly has removed this requirement.

(9) HIERARCHY OF ALLOCATION BASES

The proposed CAS 418 provided, in § 418.50(b), a list of alternative allocation measures. The proposal would have required the use of the "best available" representation of resource consumption. Commentators questioned the need for an expressed preference and suggested a free choice among the allocation bases listed.

The Board believes that the establishment of the hierarchy is essential to assure that the basic concept of cost allocations as expressed by the Board in its statements of policy and in other Standards promulgated to date is achieved. The Board, however, made revisions to the Standard to lessen the concerns expressed by commentators. First, instead of the "best available representation of resource consumption," the Board has substituted therefor, in § 418.50(e), the phrase "an appropriate measure of resource consumption." The Board also provided that the determination of which allocation measures to be used must be made on the basis of the individual circumstances, including the availability and quality of the data on which the potential measures are based.

(10) USE OF AN ALLOCATION BASE REPRESENTATIVE OF THE ACTIVITY BEING MANAGED OR SUPERVISED

A number of commentators questioned when the fourth step of the hierarchy in the proposed CAS 418, a base representative of the activity being managed or supervised, was to be used. The Standard has been revised to provide more clearly that this type of base is to be used only to allocate indirect cost pools containing significant amounts of the costs of management or supervision of activities involving direct labor or direct material cost, which are direct costs as defined by the Board. Therefore these cost pools are those which include the costs of managing and supervising final cost objectives or other cost objectives which are accounted for in a similar manner (those listed in § 418.50(d)(3)). A base representative of the activity being managed or supervised is not suitable for the allocation of the costs of management or supervision of activities involving only indirect costs.

For emphasis, the fourth step of the hierarchy has been set forth in a paragraph, § 418.50(d), separate and apart from the first three steps of the hierarchy (§ 418.50(e)) which should be used for allocating other indirect cost pools such as service centers.

(11) CROSS-ALLOCATION AMONG INDIRECT COST POOLS

The March 16, 1978 publication provided that only a cross-allocation or a sequential method could be used. In response to that proposal, commentators suggested that any method that would give the appropriate result be permitted.

The proposed CAS 418 in the July 23, 1979 publication provided for the use of any allocation method which would not result in significantly different allocation from that which would be obtained through using cross-allocation. A number of commentators stated that this provision was too complicated and costly. The Board continues to believe that the Standard should require the use of methods which would provide a reasonable representation of the beneficial or causal relationship existing among indirect cost pools. The Board was persuaded to broaden the test so that this relationship can be achieved by the use of any method that would approximate either the cross-allocation or the sequential method. Accordingly, revisions were made to § 418.50(e)(4) to permit such alternative methods.

(12) CASUAL SALES

A number of commentators suggested that the proposed CAS 418 should specifically allow casual sales of services to be costed at other than full cost. Contractor definition and classification of sales as casual sales varies considerably among contractors. The Board has found no clear and consistent criteria for distinguishing these sales activities other than on the basis of materiality. The Board is of the opinion that for sales to be characterized as casual, they must be an immaterial part of the total activities of a cost pool. The Board expresses again its position that it will not deal with insignificant items of cost. Under the circumstances, the contracting parties can determine the acceptability of the costing methods to be used. Where sales represent a material part of the total activities of a cost pool, they cannot be deemed to be casual.

(13) DEFINITION OF PRODUCTIVE ACTIVITY

In the proposed CAS 419, the term "productive activity" was important to the determination of the number of pools which would be required for the allocation of overhead costs. Commentators expressed concern that the proposal would result in unnecessary proliferation of overhead pools because of the definition which was provided. The Standard has been revised to provide for the determination of the number of pools based on the concept of homogenity.

(14) ACCOUNTING FOR THE COSTS OF SPECIAL FACILITIES

The Standard being promulgated today does not provide guidance for accounting for the costs of special facilities (e.g., space chambers, wind tunnels, reactors) accumulated in separate indirect cost pools. These assets usually do not have application to all of the work of a business unit, and this circumstance creates difficult questions concerning the appropriate cost allocation techniques to be applied. The Board recognizes a need for particular attention to the accounting for the limited number of special facilities involved and has established a project in this area to review the cost allocation issues.

(15) DEGREE OF SPECIFICITY IN PROPOSED CAS 419

As discussed previously, a large number of commentators expressed concern that the definition of "productive activity" and the 5 percent materiality test which were included in the proposed CAS 419 could result in unnecessary proliferation of overhead pools. A large number of commentators were also critical of the proposed CAS 419 because in their opinion it provided too great a degree of specificity. The requirements relative to separate overhead pools, the specific reference to the treatment of costs of special facilities, and the treatment of purchased labor and overtime premiums and shift differentials in allocation bases were considered by many commentators to be too procedural and detailed.

The Board was of the opinion that some degree of specificity would be desirable and necessary in this area to minimize differing interpretations by the contracting parties. In light of the number of criticisms on the specificity of the proposed CAS 419, however, the Board decided to remove the references to those terms and provisions. The elimination of these terms and provisions does not reflect a change in position concerning the appropriate accounting for the costs involved. Rather, in consolidating the proposed 417, 418 and 419 into a single CAS 418 being promulgated today, the Board is providing a more general Standard incorporating the basic concepts of cost allocation previously established in the Board's *Restatement of Objectives, Policies and Concepts.*

(16) EVALUATION OF BENEFITS AND COSTS

Many commentators asserted that the costs of implementing the proposed Standards would outweigh the benefits that would be derived from them. They were concerned that the Standards would require significant accounting changes because of the perceived detailed prescriptions in the Standard and for the potential implementation of changes in cost accounting practices where no material cost impact would result. The Board believes the Standard being promulgated today will significantly reduce the anticipated costs of implementation as compared with the prior proposals. This has been accomplished by reducing the degree of specificity and by emphasizing the importance of materiality in determining when changes in cost accounting practices are required. These revisions should minimize the potential for excessive proliferation of cost pools. The Board notes that this

Standard is applicable to a significant percentage of the total costs of negotiated defense contracts. The provisions of this Standard will provide greater assurance of uniformity and consistency in accounting for these costs than was previously available. The Board believes that the benefits of the increased uniformity and consistency in cost allocation which will result from the Standard outweigh the costs of implementation.

Title 4 CFR Chapter III is amended by adding a new Part 418 to read as follows:

PART 420—ACCOUNTING FOR INDEPENDENT RESEARCH AND DEVELOPMENT COSTS AND BID AND PROPOSAL COSTS

Sec.
420.10 General applicability.
420.20 Purpose.
420.30 Definitions.
420.40 Fundamental requirement.
420.50 Techniques for application.
420.60 Illustrations.
420.70 Exemptions.
420.80 Effective date.

PREAMBLE A

AUTHORITY: 84 Stat. 796, sec. 103 (50 U.S.C. App. 2168).

SOURCE: 44 FR 55127, Sept. 25, 1979, unless otherwise noted.

EDITORIAL NOTE: A supplement, consisting of the preamble to these regulations as they appeared in the FEDERAL REGISTER, follows the text of this part. This preamble is intended to explain the regulations in nontechnical language.

The preamble to the original publication of this part (44 FR 55127, Sept. 25, 1979) is set forth in preamble A of the supplement.

§ 420.10 General applicability.

General applicability of this Cost Accounting Standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the Cost Accounting Standards contract clause in negotiated defense prime contracts and subcontracts. (§ 331.30 of this chapter.)

§ 420.20 Purpose.

The purpose of this Cost Accounting Standard is to provide criteria for the accumulation of independent research and development costs and bid and proposal costs and for the allocation of such costs to cost objectives based on the beneficial or causal relationship between such costs and cost objectives. Consistent application of these criteria will improve cost allocation.

§ 420.30 Definitions.

(a) The following definitions of terms which are prominent in this Standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this Standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Allocate.* To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Bid and proposal (B&P) cost.* The cost incurred in preparing, submitting, or supporting any bid or proposal which effort is neither sponsored by a grant, nor required in the performance of a contract.

(3) *Business unit.* Any segment of an organization, or an entire business organization which is not divided into segments.

(4) *General and administrative (G&A) expense.* Any management, financial, and other expense which is incurred by or allocated to a business unit and which is for the general management and administration of the business unit as a whole. G&A expense does not include those management expenses whose beneficial or causal relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

(5) *Home office.* An office responsible for directing or managing two or more, but not necessarily all, segments of an organization. It typically establishes policy for, and provides guidance to the segments in their oper-

ations. It usually performs management, supervisory, or administrative functions, and may also perform service functions in support of the operations of the various segments. An organization which has intermediate levels, such as groups, may have several home offices which report to a common home office. An intermediate organization may be both a segment and a home office.

(6) *Independent research and development (IR&D) cost.* The cost of effort which is neither sponsored by a grant, nor required in the performance of a contract, and which falls within any of the following three areas:

(i) Basic and applied research,

(ii) Development, and

(iii) Systems and other concept formulation studies.

(7) *Indirect cost.* Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(8) *Segment.* One of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this Standard: None.

§ 420.40 Fundamental requirement.

(a) The basic unit for the identification and accumulation of IR&D and B&P costs shall be the individual IR&D or B&P project.

(b) IR&D and B&P project costs shall consist of all allocable costs, except business unit general and administrative expenses.

(c) IR&D and B&P cost pools consist of all IR&D and B&P project costs and other allocable costs, except business unit general and administrative expenses.

(d) The IR&D and B&P cost pools of a home office shall be allocated to segments on the basis of the beneficial or causal relationship between the IR&D and B&P costs and the segments reporting to that home office.

(e) The IR&D and B&P cost pools of a business unit shall be allocated to the final cost objectives of that business unit on the basis of the beneficial or causal relationship between the IR&D and B&P costs and the final cost objectives.

(f) (1) B&P costs incurred in a cost accounting period shall not be assigned to any other cost accounting period.

(2) IR&D costs incurred in a cost accounting period shall not be assigned to any other cost accounting period, except as may be permitted pursuant to provisions of existing laws, regulations and other controlling factors.

§ 420.50 Techniques for application.

(a) IR&D and B&P project costs shall include: (1) Costs, which if incurred in like circumstances for a final cost objective, would be treated as direct costs of that final cost objective, and (2) the overhead costs of productive activities and other indirect costs related to the project based on the contractor's cost accounting practice or applicable Cost Accounting Standards for allocation of indirect costs.

(b) IR&D and B&P cost pools for a segment consist of the project costs plus allocable home office IR&D and B&P costs.

(c) When the costs of individual IR&D or B&P efforts are not material in amount, these costs may be accumulated in one or more project(s) within each of these two types of effort.

(d) The costs of any work performed by one segment for another segment shall not be treated as IR&D costs or B&P costs of the performing segment unless the work is a part of an IR&D or B&P project of the performing segment. If such work is part of a performing segment's IR&D or B&P project, the project will be transferred to the home office to be allocated in accordance with paragraph (e) of this section.

(e) The costs of IR&D and B&P projects accumulated at a home office shall be allocated to its segments as follows:

(1) Projects which can be identified with a specific segment(s) shall have their costs allocated to such segment(s).

(2) The costs of all other IR&D and B&P projects shall be allocated among all segments by means of the same base used by the company to allocate its residual expenses in accordance with 4 CFR Part 403; provided, however, where a particular segment receives significantly more or less benefit from the IR&D or B&P costs than would be reflected by the allocation of such costs to the segment by that base, the Government and the contractor may agree to a special allocation of the IR&D or B&P costs to such segment commensurate with the benefits received. The amount of a special allocation to any segment made pursuant to such an agreement shall be excluded from the IR&D and B&P cost pools to be allocated to other segments and the base data of any such segment shall be excluded from the base used to allocate these pools.

(f) The costs of IR&D and B&P projects accumulated at a business unit shall be allocated to cost objectives as follows:

(1) Where costs of any IR&D or B&P project benefit more than one segment of the organization, the amounts to be allocated to each segment shall be determined in accordance with paragraph (e) of this section.

(2) IR&D and B&P cost pools which are not allocated under paragraph (f)(1) of this section, shall be allocated to all final cost objectives of the business unit by means of the same base used by the business unit to allocate its general and administrative expenses in accordance with 4 CFR 410.50; provided, however, where a particular final cost objective receives significantly more or less benefit from IR&D or B&P costs than would be reflected by the allocation of such costs the Government and the contractor may agree to a special allocation of the IR&D or B&P costs to such final cost objective commensurate with the benefits received. The amount of special allocation to any such final cost objective made pursuant to such an agreement shall be excluded from the IR&D and B&P cost pools to be allocated to other final cost objectives and the particular final cost objective's base data shall be excluded from the base used to allocate these pools.

(g) Notwithstanding the provisions of paragraphs (d), (e) or (f) of this section, the costs of IR&D and B&P projects allocable to a home office pursuant to § 420.50(d) may be allocated directly to the receiving segments, provided that such allocation not be substantially different from the allocation that would be made if they were first passed through home office accounts.

§ 420.60 Illustrations.

(a) Business Unit A's engineering department in accordance with its established accounting practice, charges administrative effort including typing to its overhead cost pool. In submitting a proposal the engineering department assigns several typists to the proposal project on a full time basis and charges the typists' time directly to the proposal project, rather than to its overhead pool. Because the engineering department under its established accounting practice does not charge the cost of typing directly to final cost objectives, the direct charge does not meet with the requirements of § 420.50(a).

(b) Company B has five segments. The company undertakes an IR&D project which is part of the IR&D plans of segments X, Y, and Z, and will be of general benefit to all five segments. The company designates Segment Z as the project leader in performing the project. In accumulating the costs, each segment allocates overhead to its part of the project but does not allocate segment G&A. The IR&D costs are then allocated to the home office by each segment. The costs are combined with other IR&D costs that benefit the company as a whole. The costs are allocated to all five segements by means of the same base by which the company allocates its residual home office expense costs to all segments. This practice meets the requirements of §§ 420.40(b), 420.50(e)(2), and 420.50(f)(1).

(c) Business Unit C normally accounts for its B&P effort by individual project. It accumulates directly allocated costs and departmental overhead costs by project. The business unit also submits large numbers of bids and proposals whose individual costs of preparation are not material in amount. The business unit collects the cost of these efforts under a single project. Since the cost of preparing each individual bid and proposal is not material, the practice of accumulating these costs in a single project meets the requirements of § 420.50(c).

(d) Segment D requests that Segment Y provide support for a Segment D IR&D project. The work being performed by Y is similar in nature to Y's normal product and is not part of its annual IR&D plan. Segment Y allocates to the project all costs it allocates to other final cost objectives, including G&A expense. Segment Y then directly transfers the cost of the project to Segment D in accordance with it normal intersegment transfer procedure. This accounting treatment meets the requirements of § 420.50(d) and 4 CFR Part 410.

(e) Contractor E has six operating segments and a research segment. The research segment performs work under (i) research and development contracts, (ii) projects which are not part of its own IR&D plan but are specifically in support of other segments' IR&D projects, and (iii) IR&D projects for the benefit of the company as a whole.

(1) The research segment directly allocates the cost of the projects in support of another segment's IR&D projects, including an allocation of its general and administrative expenses, to the receiving segment. This practice meets the requirements of § 420.50(d).

(2) The costs of the IR&D projects which benefit the company as a whole exclude any allocation of the research segment's general and administrative expenses and are transferred to the home office. The home office allocates these costs on the same base it uses to allocate its residual expenses to all seven segments. This practice meets the requirements of § 420.50(e)(2) and (f)(1).

(f) Company F accumulates at the home office the costs of IR&D and B&P projects which generally benefit all segments of the company except Segment X. The company and the contracting officer agree that the nature of the business activity of Segment X is such that the home office IR&D and B&P effort is neither caused by nor provides any benefit to that segment. For the purpose of allocating its home office residual expenses, the company uses a base as provided in 4 CFR Part 403. For the purpose of allocating the home office IR&D and B&P costs, the company removes the data of Segment X from the base used for the allocation of its residual expenses. This practice meets the requirements of § 420.50(e)(2).

(g) Company G has 10 segments. Segment X performs IR&D projects, the results of which benefit it and 2 other segments but none of the other seven segments. The cost of those projects performed by Segment X are transferred to the home office and allocated to the three segments on the basis of the benefits received by the three segments. This practice meets the requirements of § 420.50(e)(1) and § 420.50(f)(1).

§ 420.70 Exemptions.

This Standard shall not apply to contractors who are subject to the provisions of Federal Management Circular 74-4 (Principles for Determining Cost Applicable to Grants and Contracts with State and Local Governments).

§ 420.80 Effective date.

(a) The effective date of this Cost Accounting Standard is March 15, 1980.

(b) This Cost Accounting Standard shall be followed by each contractor as of the start of his second fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

PREAMBLE A

Preamble to Original Publication, 9-25-79

The following is the preamble to the original publication of Part 420, 44 FR 55127, Sept. 25, 1979.

(1) BACKGROUND

Work on the development of this Standard was initiated based on the General Accounting Office *Report on the Feasibility of Applying Uniform Cost Accounting Standards to Negotiated Defense Contracts.* The report referenced problem areas concerned with (1) the allocation of incurred costs to IR&D and B&P projects, (2) the allocation of such costs to cost objectives, and (3) the definition of IR&D and B&P work tasks. Over the years, Congress has continued to express its concern about the large amount of money reimbursed to defense contractors in the area of IR&D and BP. In 1978, the last reported year, the 90 companies large enough to have advance IR&D and B&P agreements with the Government, were reimbursed by the Government about $1.2 billion for this effort.

Early research conducted by the Board was directed towards obtaining information on the views, policies, definitions, accounting practices and administrative procedures followed in the management of IR&D and B&P activities by the defense industry, commercial companies, and Government agencies. This research was accomplished by means of questionnaires sent to 65 defense contractors and 10 commercial companies; reviews of General Accounting Office reports, congressional hearings, Armed Services Board of Contract Appeals cases, various technical papers; and discussion with several Government agencies. Also included in the research were evaluations of recommendations made by a study group of the Commission on Government Procurement covering IR&D costs and a Statement concerning the *Accounting for Research and Development Costs* (FAS No. 2) issued by the Financial Accounting Standards Board.

A research draft was distributed on April 29, 1977, to obtain comments. Comments were received from 73 respondents. The Board after considering the comments published a proposed Standard for comment in the FEDERAL REGISTER on July 28, 1978. Sixty-three commentators responded to this publication. Because significant revisions appeared appropriate after evaluation of the comments, the Board decided to publish the proposed Standard for comments a second time in the FEDERAL REGISTER on May 25, 1979. 46 responses were received from individual companies, Government agencies, professional associations, public accounting firms, industry associations and others. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by organizations and individuals have resulted in a number of changes in the Standard. The comments below summarize the issues discussed in connection with both proposed Standards and explains major changes which have been made to the earlier proposals. This Standard was previsouly published as CAS 422. It has been renumbered to CAS 420 to accommodate changes in the work plans of the Board.

(2) NEED FOR A STANDARD

Many commentators questioned the need for a separate Standard for IR&D and B&P. Almost all of those who raised this issue cited the other allocation Standards, 403 and 410 and proposed indirect cost Standards 417, 418 and 419 and stated that the allocation practices set forth in those Standards adequately cover the allocation of IR&D and B&P costs.

Appendix III of the General Accounting Office Cost Accounting Standards feasibility study is entitled "Problem Areas in the Assignment of Government Contract Costs." It contained a tabulation of problem areas. The subject of "IR&D/B&P/Economic Planning" represented the highest number of reported problems of the 23 subjects on the list. On that list also were the subjects of "allocation", "direct vs. indirect", depreciation, etc. An analysis of disclosure statements in the Cost Accounting Standards

Board's data bank showed a considerable divergence in accounting practices followed by Government contractors. For example, the disclosure statements revealed that contractors allocated IR&D and B&P cost pools to final cost objectives by means of such allocation bases as sales, cost of sales, cost input, modified cost input, modified cost of sales, direct labor dollars, manhours, and headcount. Staff research which involved visits with over 50 defense contractors and several Government agencies confirmed this divergence of practice. DOD and NASA have similar procurement regulations covering the accounting for these costs, but other agency regulations vary substantially and, as a result, a variety of accounting practices are in use for IR&D and B&P costs.

This Standard will provide for increased uniformity and consistency of allocation among segments based o.. the beneficial or casual relationship between the IR&D and B&P costs and segments of a company. The Standard will also provide for increased uniformity in the composition of these costs within contractor's segments, especially in the segments identified as central research laboratories.

The Board recognizes that the already promulgated allocation Standards 403 and 410, and the proposed indirect cost Standards 417, 418 and 419 have general requirements which will be consistent with the requirements of this Standard. Standards 403 and 410, however, would each have to be amended to include the specific accounting provisions of this Standard. IR&D and B&P costs are an important element of the contractor's total costs allocated to its final cost objectives. The Board believes that the accounting practices for these costs should be centralized in a single Standard in order to clearly provide the proper guidance for their allocation to cost objectives. Neither the contractor nor the Government should have to search out the accounting requirements in various Standards in order to obtain this guidance. By providing this guidance in a single source the Board believes that the administrative and accounting complexities for these costs will be reduced for both the contractor and the Government.

(3) DEFINITIONS

Several commentators continue to raise questions regarding the definitions. The comments generally requested definitions to clarify the accounting for "B&P administrative costs" and "technical" effort associated with IR&D costs. The words requested to be included in the Definition of Bid and Proposal Costs are: "B&P administrative costs, when not separately identified and classified as B&P costs in accordance with the contractor's normal accounting practice, are not considered B&P costs for the purpose of this Standard." Commentators also suggested that the word "technical" be included in the definition of IR&D effort so as to determine the nature of the costs allocable to IR&D effort. The commentators wanted these changes as an aid in determining what costs should be charged directly to these projects.

The definitions of IR&D costs and B&P costs are not intended to include allocation requirements. Guidance on allocation is included in other sections of the Standard. Section 420.50(a)(1) of the Standard provides guidance on what costs are to be charged directly to IR&D and B&P projects. Therefore, the requested additions are not necessary.

(4) ACCUMULATION OF IR&D COSTS AND B&P COSTS BY PROJECT

A few respondents commented on the requirement in the Standard to account for IR&D and B&P costs by project. One commentator stated that he believed that most contractors who will be required to comply with this requirement have the capability to accumulate IR&D and B&P costs by individual projects. The commentator noted that the Board has properly considered the concept of materiality by permitting the combining of the costs of IR&D or B&P efforts of small dollar value in a single project for inclusion in the appropriate pool without the necessity of separate cost identification.

One commentator stated that even though it accounted for IR&D and B&P costs by project, it was certain that there were small contractors who did not have systems which would be sophisticated enough to keep costs in such a way. The staff of the Board visited in excess of 50 contractors in conducting research on this project. In every instance contractors accumulated the costs of IR&D and B&P by project. The Board believes that, with the materiality consideration provided in § 420.50(c), the requirement to accumulate IR&D and B&P costs by project should be retained. In further consideration of the materiality concept, overhead costs and other indirect costs allocable to individual IR&D and B&P projects need not be recorded by individual project if subsequent pool allocations of these costs yield the same results as if they had been so recorded.

It was noted that the reference to "clearly and exclusively" as the criteria for allocating costs directly to IR&D and B&P projects makes a more limited requirement for this allocation than is provided for in proposed Standard 417, Distinguishing between Direct and Indirect Costs. The Board's intent is to be consistent in the accounting specified for costs incurred in like circumstances, and the use of the terms "clearly and exclusively" in the fundamental requirement was intended to provide this consistent treatment. It was pointed out that the same test which is included in proposed Standard 417 is only one of three tests for making the determination of what cost shall be accounted for as a direct cost.

The Board agrees that the use of "clearly and exclusively" in this Standard without the use of the complete set of criteria would have placed a limitation on what costs should be allocated directly to IR&D and B&P projects, and this would be more restrictive than the requirement contained in proposed Standard 417. The Board believes that it would be inappropriate to restate in CAS 420 the entire fundamental requirement for the proposed Standard on Distinguishing Between Direct and Indirect Costs. It believes further that the techniques for application, § 420.50(a)(1) adequately establish the allocation requirement sought for these costs. For all of these reasons, the fundamental requirement paragraph has been revised accordingly.

(5) ALLOCATION OF BUSINESS UNIT G&A EXPENSES TO IR&D AND B&P COSTS

One commentator raised the question of allocating business unit general and administrative expenses to IR&D and B&P costs. This commentator made the point that accounting for this effort by project is tantamount to treating it as a final cost objective and therefore it should have allocated to it a business unit's general and administrative expenses. Both proposals published in the FEDERAL REGISTER, July 28, 1978 and May 25, 1979, contained the provision that business unit G&A expenses should not be allocated to IR&D and B&P costs. A majority of respondents to the July 28, 1978 proposal commented favorably on that section of the proposal.

Many of these commentators in replying to an earlier draft of the Standard, which had provided for allocating G&A expenses to IR&D and B&P costs, had expressed the view that IR&D and B&P costs were of general benefit to a segment or a company and therefore similar in nature to G&A expenses. They believed that since such costs were similar in nature to G&A expenses they should not receive an allocation of G&A expenses. The Board was pursuaded by this view and for that reason the Standard retains the provisions for not allocating business unit general and administrative expenses to IR&D and B&P costs.

Several commentators directed remarks to accounting for IR&D and B&P costs at organizations of a company that perform as research laboratories. Some stated the belief that G&A expenses of such segments should be allocated to its IR&D costs if the segment is a "central research laboratory." Others, including an industry association, were of the opinion that a research laboratory should be treated as any other segment and its IR&D costs should not receive an allocation of G&A expenses.

The Board for some time has been persuaded that the nature of IR&D and B&P effort is such that it should not receive an allocation of business unit G&A expenses. Nothing in the comments received from the three commentators seeking to have special IR&D or B&P costs accounted for differently than all other IR&D or B&P costs provided the Board with criteria for setting up different accounting treatment. The Board believes that such costs should not receive an allocation of business unit G&A expenses and the Standard so provides.

(6) ALLOCATION OF G&A EXPENSES TO WORK PERFORMED BY ONE SEGMENT FOR ANOTHER SEGMENT OR HOME OFFICE

Many contractors in responding to the proposed Standard objected to the provisions in the proposed Standard which required that G&A expenses be allocated to work performed by one segment for another segment or home office. Some stated the belief that § 420.50(c) was inconsistent with § 420.40(c) in the proposed Standard, which provided that business unit G&A expenses shall not be allocated to IR&D and B&P projects. The Board sees no inconsistency. If the work performed is an IR&D or B&P project of the performing segment and also benefits the receiving segment, it must be transferred to the home office without an allocation of business unit G&A expenses in accordance with § 420.50(f)(1). It will then be allocated to benefiting segments pursuant to § 420.50(e). If the work is not IR&D or B&P effort of the performing segment the allocation of general and administrative expenses will be governed by CAS 410.

Commentators also expressed concern that including G&A expenses in the costs of IR&D or B&P work performed by one segment for another might push total IR&D and B&P costs above the negotiated ceilings. They contended that this would make the excess cost unrecoverable from any source. Furthermore, by increasing the allocated cost of a given research effort, less research would be financed by a given research allowance.

The Board recognizes these objections, but believes that the question of whether and how G&A expenses should be allocated must be decided on other grounds. The Board believes that if work is performed at a segment and sold to or transferred to another segment directly, it should be considered a final cost objective of the performing segment. Allocating G&A expenses to such work would be consistent with CAS 410 which provides for allocating general and administrative expenses to stock or product inventory as well as to final cost objectives of the segment. This accounting treatment is consistent with previous Standards and proposals which have dealt with segments as separate units, each with their own final cost objectives. It is also consistent with proposed Standard 419.

Some commentators agreed with the concept of allocating G&A expenses to work which is part of a segment's normal product or service and therefore a final cost objective of the segment, but disagreed with the use of the phrase "project in which the performing segment has an interest." The commentators believed that the phrase was not sufficiently objective to be properly administered.

The Board recognizes that there are valid objections to the use of the descriptive phrase "has an interest (in)." This paragraph (now numbered § 420.50(d)) has been revised to provide that work performed by one segment for another shall not be treated as IR&D or B&P effort of the performing segment unless the work is also part of an IR&D or B&P project of the performing segment.

(7) ALLOCATION OF HOME OFFICE IR&D AND B&P COST POOLS

In being responsive to comments on earlier proposals, the May 1979 proposal provided for allocation of IR&D or B&P costs to a limited group of segments or to specific segments where such identification could be established between specific work and benefiting or causing segments. At the urging of most commentators, the identification requirements and the base for allocation were stated as general requirements in the proposal. Two commentators suggested language to provide that a clear and exclusive identification of work to a specific segment(s) should be required to permit this type of allocation. The Board believes that such a change would be unduly restrictive.

The Board is aware that usually not all IR&D or B&P costs could be identified to specific segments. The Board believes that such residual home office IR&D and B&P costs should be allocated on a base which is representative of the total activity of segments being managed. Cost input therefore was selected in the May 1979 proposal as a good representation of total activity.

Several commentators objected to the use of only one base. As stated previously, the Board is seeking a base that will represent the total activity of the segments reporting to the home office. It does not with the Standard to be needlessly restrictive. The base used to allocate the home office residual expense under CAS 403 is a base representing total activity. A majority of commentators to the proposed Standard suggested that, in lieu of cost input as the base, the company be allowed to allocate residual home office IR&D and B&P costs on the same base it now uses to allocate home office residual expense under CAS 403. The Standard has been revised to provide for that method of allocation, but the amount of IR&D and B&P costs so allocated is not to be added to the residual pool to determine whether use of the 3 factor formula in CAS 403 is required.

One commentator recommended that "* * * all IR&D costs be pooled at the home office level and then allocated in a consistent and uniform manner over the entire business. This policy would serve as a deterrent to contractors undertaking frivolous IR&D projects or projects of questionable military relevance in divisions where costs would otherwise be borne primarily by the Government."

Early in its research the Staff considered this approach to determine if it best represented the beneficial or causal relationship between the IR&D and B&P costs and final cost objectives. The staff found that it was not unusual to find IR&D or B&P efforts which were clearly of benefit to or caused by a single segment or a group of segments within a company. For that reason the Board believes that the beneficial or causal relationship between IR&D and B&P costs and final cost objectives can be more effectively identified at organization levels below the one encompassing the entire company.

There may be situations where the beneficial or causal relationship can best be reflected by pooling and allocating on a general basis over the entire company. In such cases, the method suggested by this commentator would be called for under the Standard.

(8) ALLOCATION OF SEGMENT IR&D AND B&P COST POOLS

Several commentators suggested that where IR&D or B&P effort is determined to be of benefit to or caused by more than one segment, direct transfer of that IR&D or B&P costs between segments should be permitted. The Standard being promulgated today continues to provide that any IR&D and B&P project which benefits more than one segment of the organization shall have its costs transferred to the home office for allocation among benefiting segments. To avoid unnecessary recordkeeping, however, the Board has provided that the transfer can be recorded directly in the accounts of the other segments if the resulting allocation is substantially the same as it would be if passed through the home office.

One commentator was concerned that there would be confusion as to the home office to which such costs would be transferred. The suggestion was made that the Standard provide that such costs be transferred to an intermediate home office. The Board believes that such an addition is not needed. The definitions of both home office and segment in 4 CFR Part 400 make clear that the transfer of costs under this provision of the Standard could be only to the home office most immediate to the segment.

(9) Allocation of IR&D and B&P Costs to Product Lines

Many commentators to the proposed Standard felt strongly in their responses that the allocation of IR&D or B&P costs to product lines would be impractical. Most commentators believed that the arguments and disagreements between the parties as to what constitutes a Product Line would outweigh any possible benefits that could be received from the direct identification of cost objectives that would be achieved by such provision.

In visits made by the Staff with several commentators subsequent to the publication of the proposed Standard, the question of using the same definition of Product Line used by the Federal Trade Commission (FTC) in its Line of Business Reporting was discussed. All the commentators were of the opinion that this definition would not be suitable in determining guidance for the allocation of segment IR&D and B&P costs to product lines. The primary concern of the commentators was that the FTC definition establishes product lines within a company that cross over several segments of the company. Consequently, contractors would face considerable difficulties in attempting to allocate IR&D and B&P costs in accordance with the FTC definition.

In further considering the question of defining Product Line, the comments on the proposal by the Department of Defense were particularly pertinent. Those comments stated that "In the case of product lines, our experience with the cost principle that was in the ASPR prior to 1970 convinced us that it is not practicable to define a product line. In our attempt to designate product lines, and relate development costs to them, we found ourselves in endless arguments with contractors. . . . In our experience we found that contractors and contracting officers could seldom agree on product lines and usually resolved the matter by describing a product line that included all work in the plant. If the product line allocation provision remains in the proposed Standard, we expect these experiences will again be repeated."

The Board has considered the problems connected with the lack of definition and the administrative effort that would accompany any attempt to allocate the costs of individual IR&D or B&P projects to product lines. These provisions are not included in the Standard being promulgated today.

(10) Selection of Allocation Base for Segment IR&D and B&P Costs

The majority of commentators objected to the use of only the total cost input base for the allocation of a segment's IR&D and B&P costs to final cost objectives. Most of these commentators suggested the Standard be revised to provide that IR&D and B&P costs be allocated to final cost objectives of the business units using the same base that is used to allocate the business unit G&A expense to final cost objectives.

The Board agrees that the beneficial or causal relationship between IR&D and B&P costs and final cost objectives is similar to the relationship between G&A expenses and final cost objectives. After considering the many comments regarding this part of the Standard, it has been revised and the allocation requirement now states that the IR&D and B&P cost pools shall be allocated to final cost objectives of the business unit using the same base that the business unit uses to allocate its G&A expenses.

(11) Deferral of Development Costs

The proposed Standard provided for the deferral of the cost of IR&D effort which met specific criteria, and established criteria for the identification of such costs. It also noted that the composition of the costs and the allocation procedure for such costs would require further research before establishing an accounting Standard. Reaction to this provision in the proposal has been extensive and varied.

Several respondents to the May 25, 1979, proposed Standard noted that the Board should not allow the allocation of deferred development costs as this would be in conflict with the Financial Accounting Standards Board's (FASB) Statement No. 2, *Accounting for Research and Development Costs.*

One of these pointed out that the FASB in its statement set forth the position that for financial reporting purposes research and development costs should be charged as a current period cost. Another stated that his company did not and would not defer such expenses, even if the Standard permitted such action.

Although the Board has always considered the FASB to be an authoritative body and considers its statements when promulgating its own, the FASB's concern is with external financial reporting, not with contract costing. FAS Statement No. 2 therefore is not determinative for contract costing and pricing purposes.

A few commentators agreed with the provision as stated in the proposal and urged its adoption without modification. One industry commentator said, "We agree with the language as stated and believe the criteria is conceptually sound so as to permit implementation by the acquisition agencies. We do not feel that further research on behalf of the CAS Staff is necessary, and (we) encourage this language be contained in the promulgated standard as written."

The majority of commentators expressed approval of the concept provided that the act of deferral should be at the sole option and discretion of the contractor. The Board has concluded that this would be inappropriate, however, because it would not be consonant with the uniformity and consistency objectives of Pub. L. 91-379.

A broad spectrum of commentators suggested that the Board not change the status quo of this category of costs of deferred development in this Standard. They suggested that the entire subject, including requirements for allocating deferred costs, should be treated in one Standard. The commentators who made this suggestion represented industry, a professional accounting association, and a Government agency.

The Board continues to believe that there are different types of development costs and that objective criteria can probably be found to identify such costs. It believes, also that an important aspect of this question is the accounting treatment, including the amortization and allocation of these costs. The existence and the allocability of deferred IR&D and deferred development costs are recognized to some degree today in various procurement regulations. Current proposals in the Federal Acquisition Regulations (FAR) increase the recognition and allowability of such costs.

Many commentators criticized the criteria listed in the May 1979 proposed Standard, but were unable to suggest other criteria that would provide the objective tests the Board believes necessary for a Standard on this subject. The Board will undertake research on a project to determine the feasibility of a Standard which will identify and provide for the accounting treatment of deferred development costs. In the interim, the agencies may continue to exercise their authority to identify and allocate such costs. To that end the Standard covers these costs in § 420.40(f)(2) which provides: "IR&D costs incurred in a cost accounting period shall not be assigned to any other cost accounting period, except as may be permitted pursuant to provisions of existing laws, regulations, and other controlling factors."

(12) TRANSITION FROM THE USE OF A COST OF SALES BASE TO A COST INPUT BASE

On commentator noted that the Standard was silent in regard to its application when a contractor was required to convert his accounting system from the use of a cost of sales base to the use of a cost input base for the allocation of a segment's IR&D and B&P costs. This commentator suggested that the Standard include a provision such as was incorporated in the appendix of CAS 410 which provided the accounting to be followed during the transition period. The Board does not believe that this Standard warrants the additional complexity of a transition method. The Board notes that the contractor and the Government may negotiate an equitable adjustment for this change as provided in § 331.50(a)(4)(A) of the Board's regulations.

(13) EFFECTIVE DATE OF STANDARD

One commentator stated that the promulgation of this Standard would require reorientation of both contractor and Government personnel who are charged with the accounting and administration of contracts. The commentator noted that the Standard should provide for an extended implementation period. The primary concern of the commentator was directed towards the negotiation of advance agreements for these costs, and the impact of this Standard on such advance agreements. The Board expects that this Standard will become effective on March 15, 1980. However, to provide adequate lead time for its applicability the Standard provides that it shall be followed by contractors as of the start of the second fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

(14) COST AND BENEFIT

The Board in taking into account the cost and benefits of the Standard being promulgated today was especially mindful of the significance, both in nature and amount, of the category of costs being considered here. In comments received regarding the proposed Standard published in the Federal Register, some commentators offered opinions as to the cost of implementing the Standard. One commentator stated the proposed Standard will have minimal impact on administrative costs. Some commentators stated that they had not estimated the amount of increased administrative costs which would result from implementation of this Standard. Based on their experience with previously promulgated Standards, these costs depend on the interpretation and implementation requirements used by the auditors and procurement officials responsible for the administration of Cost Accounting Standards. Two commentators provided large cost estimates for implementing this Standard. One commentator based its estimate on the requirement to identify IR&D or B&P projects to product lines. This requirement has been eliminated from the Standard being promulgated.

As mentioned earlier, Congress continues to express its concern regarding the large reimbursements defense contractors receive in order to carry out their IR&D and B&P efforts. (About $1.2 billion in 1978). As many commentators pointed out, this area of costs (especially IR & D) receives much attention through the medium of advance agreements. These advance agreements contain some accounting ground rules to be followed by the contractor in determining what constitutes IR&D and B&P costs. The current acquisition regulations, however, allow significant flexibility in determining costs for these projects. One of the benefits of the Standard is that it provides increased uniformity and consistency in determining how IR&D and B&P costs are constituted, and how these incurred costs should be allocated to cost objectives.

(15) AMENDMENTS

In addition to the promulgation of 4 CFR Part 420, related amendments to 4 CFR Part 400 and to Standards 4 CFR Part 403 and 4 CFR Part 410 are being promulgated.

FINDING AIDS

A list of CFR titles, subtitles, chapters, subchapters and parts and an alphabetical list of agencies publishing in the CFR are included in the CFR Index and Finding Aids volume to the Code of Federal Regulations which is published separately and revised annually.

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